REAUTHORIZATION OF THE FTC

HEARINGS

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

REAUTHORIZATION OF THE FEDERAL TRADE COMMISSION

MARCH 18 AND 19, 1982

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REAUTHORIZATION OF THE FEDERAL TRADE COMMISSION

THURSDAY, MARCH 18, 1982

U.S. Senate,
Committee on Commerce, Science, and Transportation,
Washington, D.C.

The committee met, pursuant to notice, at 9:48 a.m., in room 235, Russell Senate Office Building, Hon. Robert Kasten presiding.

Staff members assigned to these hearings: Lawrence R. Fullerton, Staff Counsel and Amy L. Bondurant, Minority Staff Counsel.

OPENING STATEMENT BY SENATOR KASTEN

Senator **Kasten**. The hearing will come to order. This morning we begin the first of 2 days of hearings on the authorization and oversight of the Federal Trade Commission.

Over the last several weeks a great variety of proposals have surfaced for changes in the FTC's mandate, including proposals to define and limit the FTC's authority over unfair or deceptive acts or practices, to exclude commercial advertising from unfairness authority, to modify the Commission's authority to seek civil penalties under section 5(m)(1)(B) of the FTC Act, to repeal intervenor funding authority, and many others.

I welcome the debate on these important issues. While a number of changes were made to the FTC Act in the Agency's last reauthorization, many issues, such as unfairness, were deferred, and a number of new ones have surfaced. We must maintain an active vigilance in our pursuit of the proper balance between consumer protection on the one hand and Federal regulatory reform on the other.

One issue that I feel strongly about is the deferral of any consideration of the FTC's antitrust mission. About 2 weeks ago I announced that legislation I am developing to reauthorize the FTC will not contain any provisions ending the FTC's traditional antitrust role, or limiting the FTC's flexible "unfair methods of competition" mandate.

As a former small businessman, I have a firm commitment to the enforcement of our antitrust laws. The market is, without doubt, our best regulator of business conduct. Especially in an era of deregulation, it is essential that Government maintain an active antitrust enforcement program to insure that markets remain adequately competitive.

I believe that major proposals that would affect fundamentally the FTC's antitrust mission must be approached cautiously and studied carefully. Considering the major economic issues confronting the Congress and the major consumer-protection issues confronting our committee with respect to the FTC authorization, I believe that consideration of these antitrust issues must be deferred.

Two bills have already been introduced in the Senate relating to the FTC reauthorization—S. 1984, sponsored by Senators McClure and Melcher, and S. 2221, introduced by Senator Cannon last Tuesday. Relying on the counsel of these Senators, and based on the testimony received today and tomorrow, I intend to introduce a bill of my own in the next few weeks.

I might add that one major issue addressed by legislation sponsored by Senators McClure and Melcher, the FTC's jurisdiction over professionals, will not be the focus of the hearings this week, even though this issue is very much a part of the authorization. We had 2 days of hearings on this subject last July, and I think the record there will be more than adequate to aid us in our deliberations on the question of FTC jurisdiction over professionals.

Senator McClure was to make a statement in support of his bill today, but unfortunately he is unable to join us. Without objection his statement will be added to the record at this point.

[The statement follows:]

STATEMENT OF HON. JAMES A. MCCLURE, U.S. SENATOR FROM IDAHO

Mr. Chairman and members of the subcommittee, I appreciate the opportunity to appear before you today to discuss the reauthorization of the Federal Trade Commission. In doing so, I want especially to call to your attention to the pending legislation; S. 1984, the "Federal Trade Commission Amendments of 1981", introduced by Senator John Melcher (D-MT) and myself.

Mr. Chairman, I commend you and the other members of this subcommittee for the thorough and thoughtful manner in which you have been approaching this important issue. Already you have had hearings on the difficult question of the FTC's involvement with the professions—and today and tomorrow you will hear from other groups having a strong interest in the Commission's activities. It will be most interesting to hear from the Commission itself and to learn the views of Chairman Miller, who comes to the FTC from an administration committed to reducing governmental burdens on all our citizens.

My concerns about the actions of the FTC have been known for some time. During the reauthorization of the FTC 2 years ago Senator Melcher and I led the effort to clarify the role of the FTC relative to State regulated professions. S. 1984 expands on that initiative and addresses other concerns that also have not been resolved.

In 1980 Congress enacted the Federal Trade Commission Improvement Act to make substantial revisions in the Commission's authority and proceedings. It was my hope then that the FTC would heed this signal and restrain in the scope of its activities. Unfortunately, even with the change in administrations, I do not believe our message has been understood. That is why, along with a bipartisan group of sponsors from your full committee, I introduced a comprehensive reform proposal which I hope you can utilize as the basis for your review of the Commission's charter.

I see three main problems with the FTC that need to be addressed. First, I think the procedures the Commission follows in investigating and prosecuting alleged violations are burdensome and unfair. They act as judge, jury and prosecutor. It is very easy to see the inherent conflicts of interest in these procedures. Its power to demand information and conduct fishing expeditions seems to be unlimited—and fundamental fairness to our citizens demands that Congress remedy such situations.

Second, the FTC has not altered its impression that it has the authority to set aside State laws. Nullification of State law is an act of the utmost concern and must be approached only with the highest regard for our Federal system of shared power among the States and the Federal Government. The FTC's actions to date in this area amply demonstrate its insensitivity to federalism. Further, there is no basis in the law for its forays against traditional State responsibilities. It is time Congress declared such involvement out of bounds for the FTC by firmly establishing that the Commission has no authority to preempt acts of our State legislatures.

Finally, I continue to be distressed that the Commission persists in attacking our Nation's professionals—lawyers, physicians, accountants, engineers and the like—who while admittedly not perfect, have served both their clients and the public interest quite admirably over the years. The FTC is not performing a useful service by subjecting them to another layer of regulation that is over and above their State licensure. Their apparent objective of reducing professionals to mere technicians is a disservice to our country and its citizens.

S. 1984 is an effort to address the kinds of fundamental problems I have just mentioned. It would inject fairness into the FTC's proceedings by requiring that it prove its case to a Federal district court and not to itself. It would ease the burden on the public by curbing the Commission's data gatherings powers—and by revising the unfairness provisions it would ensure against the Commission's initiating spurious actions. (I note that, according to media reports, this particular change is one sought even by the FTC's Chairman himself.) And as I have previously indicated, it would protect the autonomy of State government from further encroachment by clearly stating that the FTC may not preempt State law and that activities consistent with State law are not within its jurisdiction.

By preserving the right of our Nation's professionals to engage in voluntary self regulation in the public interest, S. 1984 would provide for the continuation of a tradition of public responsibility that has served the country well. The bill would achieve this by stipulating that State regulated professions and their nonprofit associations are not within the FTC's scope of authority. This step would not be an invitation to professionals to disregard regulations since there is substantial other law, both Federal and State, to curb any illegal behavior should it occur.

Mr. Chairman, I realize that the administration has not yet taken a position to reform the FTC, but I believe our legislation is something the President could wholeheartedly support. It would ease Federal regulatory burdens—a major goal of this administration—while preserving the balance between State and Federal Government and moving power and resources back to the States, something which President Reagan is committed. And by encouraging professional self regulation, S. 1984 is also consistent with the administration's reliance on the private sector.

Again, I would like to thank this subcommittee for allowing me to share my views on this important matter. I believe S. 1984 addresses major issues of public policy in a constructive way that is consistent with the new direction that this country is taking. Moreover, its adoption would settle the acrimonious debates that have surrounded the FTC in recent years, thus freeing the Commission from political disputes so that it can devote its energies to fair and effective enforcement of the law. I don't pretend to have all the answers and I am not an expert in this area, but I do feel very strongly that ours is a proposal worthy of your close study and consideration.

Senator **Kasten**. Senator Ford, do you have an opening statement?

Senator **Ford**. No, Mr. Chairman, I do not have an opening statement. However, I do have a statement by Senator Cannon which I ask be included in the record.

Senator **Kasten**. Without objection, Senator Cannon's statement will be included in the record at this point.

[The statement follows:]

Opening Statement by Senator Cannon

Mr. President, I introduced legislation yesterday which would make several amendments to the Federal Trade Commission Act. This bill is intended to clarify the authority of the FTC and to address a number of issues which were not resolved in the 1980 FTC Act.

Mr. President, I believe that the FTC has an important mission to protect consumers against fraud and other abusive practices and to ensure a competitive marketplace free from unreasonable restraints on trade. The bill I introduced yesterday contains no wholesale exemptions from the authority of the Commission; rather, it attempts to define and clarify the authority the Commission may exercise. This bill responds to the criticism of scholars and businessmen that Congress has given regulatory agencies broad, vague and undefined powers and insufficient guidance regarding the actions these agencies are expected to undertake.

The bill would define the Commission's authority to act against unfair methods of competition. It is very clear from the Supreme Court's decision in 1972 in the *S & H* case that the Commission is entirely free to go beyond the principles enshrined in either the letter or the spirit of the antitrust laws. 405 U.S. at 244. The definition proposed in the bill provides that "unfair methods of competition" means conduct that is inconsistent with the principles of the Sherman Act or the Clayton Act and would carry forward the Commission's authority to enforce the Robinson-Patman Act. This definition is not intended to, and would not prevent, the FTC from carrying out its antitrust mission. The definition is gounded in well developed principles of current antitrust law. It would not affect the authority of the FTC to aggressively pursue anticompetitive mergers and acquisitions or the Commission's authority to protect small businesses under the Robinson-Patman Act.

As many of you know, just a year ago the Reagan Administration proposed the abolition of the FTC's antitrust authority. A number of legal scholars have endorsed that view. This bill rejects that view and instead reaffirms the Commission's antitrust mission.

Mr. President, my bill would also define the Commission's authority to take action against "unfair acts or practices." The bill incorporates the essence of the Commission's own proposed definition of the elements of conduct constituting unfair acts or practices. There has been considerable concern regarding the unbridled authority of a majority of sitting commissioners to define whatever conduct they personally feel should be prohibited as an unfair act of practice.

Mr. President, I do not believe that any agency should be given such broad discretion to establish regulations according to their own personal views of sound policy. It is incumbent upon the Congress to establish clear and objective criteria to utilize in enforcing the FTC Act.

Before turning to the specific provisions of this legislation which I will explain briefly, let me just say that I would not claim that every element of this bill is perfected at this point and I would encourage those who are supporters as well as critics of the Federal Trade Commission to comment on the strengths or weaknesses of this bill and to point out better alternatives if they have them. But I will emphasize again that I feel it is incumbent upon the Congress to define as clearly as possible the authority of regulatory agencies and to provide the clearest guidance possible to those who are empowered to enforce our laws.

Mr. President, let me now outline the principal provisions of the bill.

First, the bill provides that the Commission will have authority to issue rules to prevent false or deceptive advertising. This will prohibit the FTC from using "unfairness" as a basis for advertising rulemaking. The Congress adopted a similar provision in 1980, and this amendment would simply make that policy permanent law. The bill would also make a similar conforming amendment to Section 5 of the FTC Act. I am aware of the concern that there is some need for "unfairness" authority to deal with ads that might encourage children to engage in unsafe conduct. I hope the hearings will focus on this issue.

A second major provision of the bill would apply the "state-action doctrine" to actions brought under Section 5 of the FTC Act alleging unfair methods of competition. This amendment will not interfere with current FTC practice, but it will remove considerable concern and doubt among many persons, including professional organizations, that the FTC might seek to assert its antitrust authority where a state has established a clear regulatory policy and where the Department of Justice would not be authorized to proceed. The amendment would simply place the FTC and the Department of Justice on an equal footing.

The third major amendment would prohibit the FTC from issuing substantive rules under such Section 6(g) of the FTC Act that are aimed at conduct that principally involves unfair methods of competition. This amendment would not affect the Commission's rulemaking authority over unfair acts or practices. The effect of this amendment would be to end a long-standing dispute over whether the FTC has any independent, substantive rulemaking authority over antitrust matters under Section 6(g). As far as I know, no significant rule exclusively directed at anticompetitive practices has ever been issued by the Commission. The octane rating rule was in essence a rule designed to prevent unfair acts or practices. And although the Commission has considered antitrust rules dealing with oil pipelines, Blue Shield plans, and other matters, they have never promulgated a pure antitrust substantive rule. I think it is quite clear from past experience that antitrust investigations are "fact intensive" and that proceeding on a case-by-case basis is a more appropriate means of enforcement. This amendment will not prevent the FTC from issuing interpretive rules and guidelines in antitrust matters. I should add that this amendment would also prevent the Commission from issuing a rule in the standards and certification rulemaking proceeding. It seems clear to me that if the Commission believes that standards groups have engaged in anticompetitive practices, the Commission should proceed against them on a case-by-case basis.

The fourth major amendment would define unfair methods of competition and unfair acts or practices. The bill would attempt to clarify the Commission's antitrust authority by defining "unfair methods of competition" to reach conduct which is inconsistent with the principles of the Sherman or the Clayton Antitrust Acts, a definition grounded in well developed principles of basic antitrust law. This would eliminate the apparently open ended authority of the FTC to go beyond the principles in either the letter or spirit of the antitrust laws which the Supreme Court appeared to affirm in the S & H case. Let me emphasize again, that in defining unfair methods of competition, we are reaffirming the FTC's antitrust mission and rejecting the proposals that the FTC's antitrust mission should be ended. And, as I mentioned, this would not affect the authority of the FTC to aggressively pursue anticompetitive mergers and acquisitions or the Commission's authority to protect small businesses under the Robinson-Patman Act. It is simply an effort to state more clearly the basic rationale for the Commission's antitrust mission.

The second major definition contained in the fourth proposed amendment would define unfair acts or practices. Unfair acts or practices are defined to include "acts or practices which have resulted in or will cause substantial injury to consumers, and such injury is neither reasonably avoidable by consumers themselves or outweighed by countervailing benefits to consumers or competition." This definition should provide a more objective test for defining unfair acts or practices. It incorporates the essence of the Commission's own policy statement of 1980 which in turn was a distillation of Commission cases and enforcement policy. This definition is not offered to restrict the Commission, or prevent them from pursuing any legitimate enforcement action.

The fifth major provision of the bill would extend the civil investigative demand procedures to the FTC's antitrust investigative authority. This amendment is merely an extension of the action taken by Congress in 1980 when it made the CID procedure applicable to investigations of unfair acts or practices. Moreover, the procedure will not prevent the Commission from obtaining any relevant evidence necessary to pursue investigations of possible unfair methods of competition. At the same time, however, it will prevent the Commission from issuing sweeping subpoenas which fail to define the purposes of the inquiry or the relevance of the evidence sought. The scope of the Commission's CID is to be the same as the antitrust civil process act and is modeled after the criteria and procedures used by the Department of Justice. Each CID must state the nature of the conduct constituting the alleged violation which is under investigation and the provision of law applicable to it. This procedure has worked well for the Department of Justice and provides a reasonable procedure for judicial review of subpoenas. However, this requirement is not intended to be overly strict or to be interpreted in a manner that would defeat the Commission's antitrust mission.

The sixth major provision of the bill would provide for Congressional review of any FTC trade regulation rule. The review procedures correct a number of technical errors in existing law and also provide for review by means of a joint resolution requiring the President's signature. This scheme will remove any Constitutional problems which have been created by recent judicial decisions overturning one or two House veto laws.

The bill also contains provisions which would put a cap on penalties which may be imposed for any single violation or series or related violations. Similar limitations on damages are contained in the laws of other regulatory agencies. The bill also provides that there is not automatic stay when a Commission order is appealed in a circuit court of appeals. The court would be authorized upon a proper showing to grant a stay. Finally, the bill provides for a three-year authorization at current funding levels, adjusted for inflation, in order to provide the Commission with adequate resources to carry out its consumer protection and antitrust mission.

Mr. President, I hope the bill I am introducing today will stimulate discussion and debate of how we can better define and clarify the authority of the Federal Trade Commission. I hope to work closely with the Chairman of the Committee, the Senator from Oregon (Mr. Packwood) with whom I have worked closely in the past, and also with the Chairman of the Consumer Subcommittee, the Senator from Wisconsin (Mr. Kasten), as well as my Democratic colleagues on the Commerce Committee, and particularly the Senator from Kentucky (Mr. Ford) who played such a leading role in our last reauthorization effort.

Mr. President, every day state legislatures enact laws to further clarify the law of wills or real estate or commercial transactions, and the Congress does the same in numerous areas. It is in that spirit that I offer this bill.

Senator **Kasten**. Senator Goldwater.

Senator **Goldwater**. I understand Senator Cannon has relieved me of the responsibility of submitting his statement for the record.

Senator **Kasten**. Senator Danforth.

Senator **Danforth**. Mr. Chairman, I do not have any opening statement. As I understand your position on not including in this reauthorization bill any diminution of the FTC's antitrust responsibility, I would agree with you in that position.

Senator **Kasten**. Our first witness today is Dr. James C. Miller, the Chairman of the Federal Trade Commission.

Jim, I would like first of all to congratulate you on your first 5 months. I think you have made great progress—the Commission has made great progress—toward the goals that you set for yourself during your confirmation last August. It is a little early, I guess, to haul you up here and put you through the reauthorization process, but the clock is running, and this is our job, so maybe I should just apologize. I appreciate your being here, and I look forward to your statement.

Chairman Miller.

STATEMENT OF HON. JAMES C. MILLER III, CHAIRMAN, FEDERAL TRADE COMMISSION

Mr. **Miller**. Mr. Chairman and members of the committee, I am very pleased to be here this morning to discuss with you the reauthorization of the Federal Trade Commission. Congressional oversight is at the heart of effective government and I am happy to be a part of it.

The goal of the FTC, now as in the past, is to foster a competitive marketplace free of unfairness and deception. I want to emphasize the commitment my fellow Commissioners and I feel to the tireless pursuit of that goal.

But experience has taught us that success in this endeavor depends crucially on two points: First, receiving appropriate legislative guidance concerning the types of initiatives the Commission should and should not undertake and, second, having the requisite tools at our disposal to be effective.

As you contemplate our agency's reauthorization, my fellow Commissioners and I respectfully ask that you give careful consideration to these two points. We also ask that you consider our views on several important matters and we welcome this opportunity to present them to you today.

Mr. Chairman and members of the committee, please bear in mind that our agency is a Commission, presently with four sitting Commissioners. The views I express today do not necessarily reflect the views of any individual Commissioners, and in some instances I will note dissenting views. But I should also note that this testimony, with its caveats, has been approved by a majority of the Commission.

Now, Senators, please let me address several of the major issues that are before this committee.

UNFAIR ACTS OR PRACTICES

The Commission has agreed—with Commissioner Pertschuk dissenting—that a more specific statutory standard with respect to "unfair acts or practices," as found in our Federal Trade Commission Act, would be appropriate. It also has agreed on the elements of such a standard.

As you know, the Commission's position with respect to unfair acts and practices is articulated in a letter of March 5, 1982, responding to an inquiry from Committee Chairman Packwood and from you, sir, Subcommittee Chairman Kasten. The Commission therein reiterated a position first stated in a December 17, 1980, letter to Senator Danforth and Senator Ford, concerning the factors the Commission considers in evaluating an act or practice alleged to be unfair. With your permission, I would like to submit copies of both of these letters for the record.[1]

Briefly, the Commission believes that unavoidable consumer injury is, and should be, the crucial elements in finding that an act or practice is unfair. In particular, the Commission believes that a statutory definition of unfairness should include three elements by which an act or practice may be evaluated.

First, the consumer injury should be substantial. The Commission's resources should not be used for the purpose of policing trivial harm. Moreover, the substantial injury should involve objective harm rather than subjective forms of harm such as social taste.

Second, the injury from the alleged unfair act or practice should outweigh its benefits. The Commission should be mindful that a given act or practice may benefit some consumers while harming others and not jump to the conclusion that an act or practice is unlawful just because some harm is associated with it.

Morever, the Commission should take account of the costs and effectiveness of any proposed remedy, monetary costs to the parties and ultimate consumers, increased paperwork and regulatory burdens, and reduced incentives for innovation and capital formation. However, to avoid excessive complication or delay in investigations, it should be admitted that in some cases a fairly subjective analysis of benefits and costs may be sufficient.

Lastly, the harm must be one which consumers could not reasonably have avoided. The Commission should confine its activities to curbing behavior that takes unfair advantage of consumers' inadequate knowledge in reaching a decision or their inability to protect themselves from such behavior.

Although both the letter of December 17, 1980, and the most recent letter of March 5, 1982, agree on the tests that should be applied to determine unfairness, the most recent letter supports the incorporation of these factors of unfairness into law, whereas the earlier letter represented only a statement of Commission policy.

DECEPTIVE ACTS OR PRACTICES

As the committee knows, section 5 of the FTC Act also addresses "deceptive acts or practices." It is my personal view, as distinguished from a Commission position, that this aspect of the Commission's jurisdiction warrants definition in the law as well.

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[1] See pp. 23 and 32.

I believe that statutory changes are necessary to correct three problems. First, the Commission currently is not required to find evidence that the challenged act or practice injures consumers. I see no reason to spend taxpayers' dollars unless consumers will be injured.

To remedy this problem . would suggest incorporating a materiality element, as does the common law. Second, the Commission should only be allowed to pursue statements or representations of fact, not of opinion.

Third, the Commission should measure deception by whether reasonable consumers are likely to be deceived, not by whether any consumers might be deceived. This does not mean that the Commission should never protect vulnerable groups. With respect to vulnerable groups, such protection could be accomplished by focusing on whether the perpetrator knew or should have known that the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived.

LEGISLATIVE VETO

In my own view, the legislative veto can be a useful means for controlling the rulemaking activities of independent agencies which are not subject to direct Presidential supervision. My fellow Commissioners, on the other hand, continue to be troubled about the policy implications of the legislative veto, consistent with the position they took during its consideration in the last Congress, but do not object to its renewal if that is the preferred congressional course.

I would only add that in view of the constitutional questions concerning legislative veto recently raised by the courts, consideration might be given to a veto provision that contains expedited procedures and includes the President.

ADJUDICATED ORDERS TO CEASE AND DESIST

Currently the statutes of other Federal agencies, including the Interstate Commerce Commission, the Environmental Protection Agency, the Civil Aeronautics Board, and the Federal Communications Commission, to name just a few, provide that cease-and-desist orders become effective 60 days after service unless stayed. However, pursuant to the FTC act, Commission cease-and-desist orders become final within 60 days only if no petition for review has been filed. Otherwise, the effective date of the entire order must await the decision of the Court of Appeals or the Supreme Court, as the case may be.

Under present law, unless the Court of Appeals grants extraordinary ancillary relief, a respondent may continue to engage in conduct which the Commission has determined unlawful until the ultimate disposition of a petition for review, which often takes years. Thus, respondents have an incentive to file petitions for review based on frivolous or other unmeritorious claims, largely for the purpose or effect of delay.

The need for this change in the law is suggested by the past record. Of all cases finally decided by a court of appeals during the 4-year period from January 1, 1977, over two-thirds of the Commission's orders were substantially affirmed. Yet the delay in the effectiveness of these affirmed orders ranged from 18 to 48 months and averaged approximately 29 months.

The Commission believes making the FTC act consistent with the other Federal statutes would reduce the incentive to file petitions for review simply for dilatory purposes. Moreover, as many challenges to Commission decisions relate only to certain provisions of a cease-and-desist order there is no compelling reason to delay the effective date of the order in its entirety.

Further, we believe that this proposed change would offer sufficient protection to those parties with legitimate reasons for noncompliance by permitting them to seek a stay of the order from the Commission, from the U.S. Court of Appeals before which a petition for review is pending, or the Supreme Court if a petition for certiorari has been filed.

To insure against delay in acting upon applications for a stay, consideration should also be given to permitting the court of appeals to consider a stay request if the Commission has not acted within 30 days from the receipt of such application.

PUBLIC PARTICIPATION FUNDING

As you know, funds have not been requested for this controversial program, beginning with President Carter's budget submission for fiscal year 1981. Despite this fact, there is disagreement among the Commissioners over continued authorization for this program. Two Commissioners wish for the authorization to be continued. One other Commissioner and I believe that this provision of the act should be deleted.

LENGTH OF REAUTHORIZATION AND FUNDING LEVEL

The Commission supports a 3-year reauthorization and does not object to the President's recommended funding levels for the pertinent years—that is, no less than $60.8 million for fiscal year 1983, $55.1 million for fiscal year 1984, and $54.6 million for fiscal year 1985.

The Commission also believes that the authorized funding levels should accommodate limited upward flexibility, for example, by 10 percent, to facilitate matters should the President and Congress wish the Commission to have more money in subsequent years. But a majority opposes authorization levels as high as contained in the existing authorization, which is $80 million for fiscal year 1982.

In conclusion, I believe that if the preceding suggestions were incorporated into law, the Commission's mission would be more carefully defined and it would have the tools to act vigorously against those whose actions are anticompetitive and injurious to consumers.

Such an approach to the control of administrative agency discretion is entirely sound, in my view. It stands in dramatic counterpoint to an entirely unsound approach that has been urged on this committee. I speak of special interest exemptions from FTC jurisdiction.

I see no basis of principle upon which one or another industry can argue that its anticompetitive, unfair, or deceptive conduct is entitled to a special exemption from the law. Of course, the law should be as clear as possible and the FTC should enforce the law fairly and rationally. But once these conditions are met, all groups should be treated equally.

It is for this reason that the Commission stated in its letter of March 5 that it fully, strongly, and unalterably opposes any amendment to exempt professionals from FTC enforcement of the antitrust and consumer protection laws of this country.

It is true that the FTC has been active in applying traditional law enforcement to the professions, but for obvious reasons. The service sector is the most rapidly growing component of our economy. In 1980, for instance, over $247 billion was spent on health care services alone. That is why the vitality of competition in this sector attracts the Commission's attention.

I do not believe the FTC can effectively accomplish its mission if such a significant sector of our economy is, by definition in law, immunized, sanctified, and set aside as a privileged class. I respectfully urge the committee to reject the professions' special appeal.

Mr. Chairman and members of the committee, that completes my prepared remarks. I shall be happy to address any questions you might have.

Senator **Kasten**. Jim, thank you.

You said that you support and the other Commissioners support the funding level being recommended by the President, which is $60.8 million. Is that correct?

Mr. **Miller**. It is a little bit more complicated than that, Senator.

Senator **Kasten**. I know I heard an $80 million figure.

Mr. **Miller**. The majority rejects the $80 million figure. A majority of the Commission can live with the figures the President has recommended. A majority also would prefer there be limited upward flexibility from those numbers, perhaps 10 percent.

Senator **Kasten**. I also appreciate your comments on the legislative veto. It would be my hope that we could extend the legislative veto part of this legislation. Maybe there are some ways that we can work with you to redefine how that process might work, but I feel strongly, and I think that the majority of the Senate will agree, that we continue to have that legislative veto.

As you know, we incorporated the veto into the Consumer Product Safety Commission reauthorization last year.

You and I know we disagree in a couple of areas—jurisdiction over professionals is one—but particularly jurisdiction over agricultural cooperatives. Generally, we do not need duplicative levels of State and Federal authority that cause more problems than they solve.

Agricultural cooperatives are regulated by the Department of Agriculture, and statutes provide limited antitrust immunities, like the Capper-Volstead Act. Frankly, here I would expect to see support for continuing—not going in any way further—the present limitation on FTC studies, investigations and prosecutions in the area of agricultural co-ops. It would be my hope that we could work to together in that area, but I certainly appreciate your point of view.

Getting back to your testimony, why have you gone beyond the Commission's recommendations regarding unfair acts or practices and made a recommendation concerning deception?

Mr. **Miller**. Well, sir, I know this is controversial, but let me just say that the only definition that we now have available for "deception" is itself circular because it says that an ad is legally deceptive if it has a "tendency or capacity to deceive." I think that is a very broad definition as well.

In fact, under this definition virtually any ad can be found to be deceptive. This possibility arises because there are virtually no limits on the kinds of claims that are actionable. There are no checks on the reasonableness of the agency's construction of the meaning of the advertising or the injury that the claim might lead to.

Now, sir, in looking at the statute it seems to me that we well should apply a concept here that is called in physics the LeChateleir principle. An illustration of that is if you have a balloon and you push on one side of it, things change on the other side of the balloon. The way things happen in the universe are solved by a system of simultaneous changes with various parameters. If you change some parameters you have to change the value of variables all over the place.

Now the Commission in the past has taken a lot of cases on the grounds of both unfairness and deception. So, if we admit there is a problem for commercial advertising with respect to unfairness, we also have to think about the possibility that the Commission might go after the same kinds of things under its deception authority. Just because everybody feels they now know what deception is does not mean that the Commission will stay within that definition in the future.

That is the reason I think it is good for Congress to make explicit the kinds of standards the Commission should have in that area.

Senator **Kasten**. Now, specifically what changes are you suggesting in this definition and what, if any, relationship to common law do the changes that you are suggesting have?

Mr. **Miller**. Well, sir, I think we should focus on a consumer injury standard in the area of deception as well. We should be mindful that certain kinds of advertising could be directed at especially vulnerable groups and make sure that the Commission has the authority so that if, for example, someone is advertising a miracle cure for cancer to an elderly population who might not be in a position to make a sound judgment, in that case I think that we should have the authority to move. But I think that we need to see that there is going to be consumer injury and it is the kind of injury consumers could not have avoided before we make a move under deception as well.

If I could, Senator, let me just give you a few examples and tell you a little bit about why these kinds of things bother me. First, the Commission has unreasonably construed claims with respect to deception. Now some of these cases were later overruled by the Commission, but let me give you a few examples.

The Commission sued a manufacturer of a hair-coloring agent for claiming that the color was permanent because it feared that some consumers might assume that the product would color hair not yet grown. It interpreted a tire brand named Safety Champion as a claim that the tire was safer than any other tire on the market. It interpreted a claim that nylon socks would last forever literally, and asked for evidence that the socks would never wear out.

It sued the California Milk Advisory Board for advertising that everybody needs milk because some people are allergic to milk, even though other government agencies have said everybody needs milk. Now those, the Commission alleged, were instances of deception.

Second, the Commission has pursued claims that were clearly statements of opinion and not of fact. It sued General Motors for advertising that Road and Track magazine concluded that the Chevy Vega was the best-handling car ever produced in America. General Motors was very taken with that and put that statement in some of its ads. But the Federal Trade Commission said you must substantiate that claim. It was not a claim that GM was making. It was somebody else who was offering that opinion. Since it could not substantiate road and track's opinion without extraordinarily elaborate tests that might not even be acceptable to the Federal Trade Commission, GM stopped putting out that ad. Now I think consumers were hurt by that. They were not given the information that one reputable car magazine concluded Vega was the best handling.

The FTC has challenged claims that yogurt is nature's perfect food that science made better—a matter over which reasonable people can surely differ. It has challenged claims that deodorant kills strongest odors despite the inherently subjective nature of that claim. It has challenged claims that a milder cigarette had a taste that was always milder. These are all examplies of the Commission challenging opinion—not fact.

Third, the Commission has pursued claims that lead to no significant injury. While the Commission must find that an advertising claim is material before it can find the claim deceptive, a claim is material if it affects any behavior. The Commission can find that there is an effect on behavior on the basis of its own expertise without any evidence at all.

The result is that the Commission brings cases where the injury to consumers, if any, is trivial. For example, claims have been held deceptive even if the implication of the claim is refuted by the product's label.

Fourth, the Commission also can find that an advertisement is deceptive for what it does not say. Although this is appropriate, when the ad creates an incorrect impression that added information can correct, the current FTC law is not so limited. Instead, it is enough that the consumers have a false belief that the advertisement fails to correct.

The Commission held it was deceptive to sell recycled oil without disclosing that it was recycled; to sell imported products without disclosing the country of origin, or to sell goods on credit without disclosing that the consumers note would be discounted to a holder-in-due-course.

In these cases it was not advertisements that led consumers to believe that oil was not recycled, that products were domestically produced, or that notes would not be discounted. Rather, these were preexisting consumer beliefs that advertising did not correct.

If the benefits of providing this information exceed the cost, then manufacturers should be required to provide it, but the Commission at the present does not engage in that balancing test. I think it should.

In short, the Commission can find an advertisement deceptive if that ad fails to correct preexisting beliefs held only by an unreasonably small portion of the population, even if it leads to no significant injury and the advertisement clearly indicates that it was conveying an opinion, not fact.

The Commission's discretion as to what is deceptive is, in a sense, virtually unlimited. Virtually any of its proposed rules regarding advertising that are now based on an unfairness doctrine could, in my judgment, be based on a deception theory. That is the reason I think it is appropriate for the Senate to give serious consideration to telling the Commission specifically what guidelines it should follow in bringing deception cases with respect to advertising.

Senator **Kasten**. My time has expired, but I just want to finish this point by asking you one final question. Does this distinction between fact and opinion mean advertisers could avoid prosecution by framing all of their claims as opinions?

Mr. **Miller**. Well, sir, I do not think so. Of course, we need some guidance from the Congress in that regard. I mean, for example, a company might say if you sign up with us and take our course you will earn $60,000 a year. Now that is a claim. That is a factual claim they are making. We would probably ask them to substantiate that.

They might say, on the other hand, if you sign up for the course we believe you will make $60,000. Now that is obviously a way to weasel out of that and we would not accept it. What we have to do is carefully delineate whether they are giving objective opinion.

An opinion is something that is not fact. Essentially you cannot test it. Whether a particular statement is a fact or an opinion is the kind of distinction that would have to be drawn.

Senator **Kasten**. Senator Ford.

Senator **Ford**. Mr. Chairman, many believe that the courts have defined deception without the Commission or the Congress outlining what deception really is. We have also heard that unfairness is in the eye of the beholder.

Mr. **Miller**. Right.

Senator **Ford**. And I do not know of many cases, if any, that have ever been won on just the single notion of unfairness. Do you know or have any documentation on cases that have been won just singularly on unfairness?

Mr. **Miller**. Well, sir, I would like to supply information for the record and let me tell you one reason I am very cautious here is, you know, sir, we are an adjudicatory agency.

Senator **Ford**. I was not sure you were going to be able to testify.

Mr. **Miller**. And I cannot really talk about some cases before us. Let me supply something for the record.

Senator **Ford**. Fine. Let me ask this question then. Where you have unfairness and deception, when you tie both of them together doesn't unfairness encompass deception?

Mr. **Miller**. Sir, what I think you are getting to is the fact that generally when we bring advertising cases we usually throw both of them in together—unfairness and deception. It is true since the Commission's authority is practically boundless with respect to what it can find as unfair, it usually makes it pretty easy for us to find something unfair, especially if it is a close call.

In other cases, when it is clearly deception we will bring the case and make the findings on the grounds of deception.

Senator **Ford**. So, on the basis of what you are saying, you could do anything you wanted to under unfairness.

Mr. **Miller**. That is right. The Supreme Court upheld that in *FTC* v. *S&H* case. The Supreme Court essentially passed on with approval statements the Commission had made as to be the basis for its unfairness standard. These, if you read them, are just extraordinarily broad and it says essentially that the Commission can find something is an unfair act or practice on basically anything three Commissioners feel is sufficient.

That gives the Commission very, very broad latitude. I think that is inconsistent with our whole notion of government. That is essentially delegating to unelected officials extraordinarily broad powers beyond those I think Congress had in mind in the beginning.

Senator **Ford**. I understand you oppose an amendment to exempt the professions and I think you stated that publicly here this morning.

What is your reaction to an amendment to clarify that the "state action" doctrine is applicable to FTC competition actions, just as it is to actions taken by the Department of Justice?

Mr. **Miller**. Well, sir, I have looked briefly at the language Senator Cannon proposed, and I think that is language that is really consistent with what we do today and consistent with the approach that I think is reasonable. It may not be needed.

On the other hand, I am not troubled by it.

Senator **Ford**. Let's talk a little bit about unfairness and deception again. If deceptive acts or practices are not defined in the reauthorization legislation that we are discussing, would you support a provision to eliminate unfairness as a basis for rulemaking in the commercial advertising area, section 18?

Mr. **Miller**. If we cannot make any changes in section 5 I would certainly be inclined toward that.

Senator **Ford**. What advertising cases have been brought strictly under unfairness in section 5?

Mr. **Miller**. Let me supply information for the record. It is usually the case that they throw in both. The Commission, in taking an advertising case, usually follows the typical approach that lawyers take, which is to throw in everything and the kitchen sink, too.

Senator **Ford**. Of course, not being a lawyer it is hard to understand how lawyers think.

Mr. **Miller**. I know, sir, I have that problem.

Senator **Ford**. How about the elimination of unfairness as a basis for case-by-case adjudication under section 5?

Mr. **Miller**. Well, if we do not have changes in section 5 of the type——

Senator **Ford**. In commercial advertising.

Mr. **Miller**. If we do not have changes of the type that I have suggested or recommended, sir, I guess I would favor the elimination of our authority over commercial advertising for section 5 in case-by-case adjudication.

Senator **Ford**. Let me ask this. What cases have been brought by the FTC say in the last 12 or 15 years that could not be brought under your proposed definition defining deceptive acts?

Mr. **Miller**. Let me give you a list of those, and I would like to have that screened by my general counsel so that I do not get into any adjudicatory matters that would disqualify me, sir.

Senator **Ford**. Mr. Chairman, I will ask one more question and then pass. This may be another question where you will have to submit it for the record, Mr. Chairman, but could you list a few examples of actual cases that could not be brought if unfair methods of competition authority was limited to the Sherman or Clayton Act violations as the chamber of commerce has suggested?

Mr. **Miller**. Let me submit that for the record. We had some preliminary indication from the chamber what their approach would be, and let me provide that answer for the record.

Senator **Ford**. Would you support such a provision?

Mr. **Miller**. Well, in a way, their provision with respect to unfair acts and practices is not far from what the Commission itself is recommending in terms of legislation.

With respect to deception, our standard I think is a little more fine tuning. It would allow us a little more flexibility, say, to address vulnerable groups.

Senator **Ford**. How about unfair methods of competition?

Mr. **Miller**. Unfair methods of competition—frankly, sir, I think that the Commission's authority in the unfair methods of competition area needs to be addressed as well.

Now, when I testified before this Committee in my confirmation hearings, I suggested that we really need to have a thorough review of our antitrust laws to see if any modernization need to take place, regarding their enforcement by the Federal Trade Commission, by the Department of Justice and by the private bar. And I still hold that view.

I think consideration might be given to at least inserting in section 4 a definition of the term "interest of the public" or "public interest" that applies to those terms as they appear in section 5(b) and elsewhere in the act. That gives a little more guidance from the Congress in the procedural aspects of the Federal Trade Commission and the procedures that the Federal Trade Commission undergoes and the things that the Federal Trade Commission takes into account in making decisions to bring complaints. Something to the effect that it should be convinced that there is a likelihood that the benefits to consumers would exceed the costs might be considered.

I do not think the Federal Trade Commission should be in the business of taking actions that actually would hurt consumers. I do not think it should be in the business of taking on cases where there is not some indication that the result would likely be in the benefit of consumers.

We have scarce resources, like all agencies, and we must allocate those properly. So I think that sort of guidance could help the Federal Trade Commission allocate its resources—a procedural technique.

Senator **Ford**. Just pursuing that one step further, in the question of unfair methods of competition would you be willing to limit the authority of the Commission to the Sherman and Clayton Act violations, as recommended by the chamber of commerce?

Mr. **Miller**. Well, actually, the language that Senator Cannon—again, I only had a chance to look at it very quickly, something in the spirit of the antitrust laws.

Senator **Ford**. I think the question I asked was somewhat different than Senator Cannon's legislation.

Mr. **Miller**. OK. Let me see if I can answer it and see if I understand the difference. The legislation I believe the chamber has proposed would be to limit our section 5 authority only to matters that were covered in sections 1 and 2 of the Sherman Act. Is that correct?

Senator **Ford**. Yes.

Mr. **Miller**. That would trouble me a bit. The reasons are that there are things that we do in filling in the gaps under unfair methods. For example, there may be a case where we would need to enjoin not only an acquiring firm, but an acquired firm in some case that did not come under section 7 of the Clayton Act. It might also be that they are just short of an act to create a monopoly or incipient collusion. We might go after it and stop something.

It is totally in the spirit of the antitrust laws, I think consistent with—if I could just go on—consistent I think with what Senator Cannon had in mind in that specific provision that he proposed. But I think we are close on that, sir.

Let me emphasize that is a personal view. Let me again, for the record, reiterate that my views on deception are not shared by the Commission, a majority of the Commission, and my view on methods of competition you asked me about, sir, is not shared by the other members of the Commission. In terms of legislation, at least.

Senator **Kasten**. I just want to interject here. It is my very strong feeling that we do not in any way back away from some of these antitrust provisions at this time.

Mr. **Miller**. If I could just elaborate on that. Surely, I am not indicating any backing off on my commitment to enforcing the antitrust laws.

I think, in answer to Senator Ford's question, the kind of thing I was suggesting would help us be more effective in pursuing the antitrust laws and restraining those kinds of activities that really are anticompetitive and hurt consumers, and not to be wasting our resources on activities that do not meet those criteria.

Senator **Kasten**. Senator Danforth?

Senator **Danforth**. Mr. Chairman, let me first ask you because I want to make absolutely clear where we are, it is my understanding that it is not your intention to redefine the antitrust portion of the FTC's authority in this reauthorization bill.

Senator **Kasten**. That is my personal preference, and I have so stated.

Senator **Danforth**. That is strongly my preference, too. So therefore, when we discuss redefining or defining unfairness in this bill, we are talking exclusively about the consumer portion of FTC jurisdiction; we are not talking about redefining or defining unfairness for the purpose of the antitrust jurisdiction of the FTC; is that correct?

Senator **Kasten**. That is my personal hope and preference. Obviously, the committee will work its will.

Senator **Danforth**. Yes. Is that your understanding of where we are, Mr. Miller?

Mr. **Miller**. Sir, except for my answer, the last answers to Senator Ford, the other discussion did not touch on unfair methods of competition. That is right.

Senator **Danforth**. So, let me say I would agree with that, and I think we should be concentrating only on the consumer protection part of the FTC's jurisdiction.

Now, with respect to defining unfairness, we had a lengthy discussion on this question several years ago when we last had an FTC authorization bill before us. And as I recall, we had a lot of colloquy on the subject as well. The thought was that unfairness was not very well defined in case law; that the use of unfairness as a basis of FTC consumer jurisdiction was a fairly new innovation on the part of the Commission, really pioneered during the Chairmanship of Chairman Pertschuk; and that therefore, rather than just have unfairness be something which was almost a subjective test, there should be a better effort to define what the meaning is. I take it that is what we are about right now.

Mr. **Miller**. Yes, sir.

Senator **Danforth**. You have proposed to us a definition of unfairness for the purpose of the consumer portion of FTC jurisdiction.

Mr. **Miller**. That is correct, and the majority of the Commission supports that.

Senator **Danforth**. And the majority of the Commission supports that.

Now, the thought, when we addressed this last time, was that we would draw upon the best thinking available, maybe consult law professors and people who had some input to offer in defining unfairness. Is it your view that the Commission, prior to presenting its definition to us, has thoroughly explored the possibilities and has drawn upon the best advice available?

Mr. **Miller**. Well, sir, I think so. Let me say it in two ways. In December of 1980, the Federal Trade Commission sent a letter to you and to Senator Ford outlining the elements of at least what they perceived to be the historical standards for unfairness. And that was based on a lot of discussion among the Commissioners and the staff and so forth.

As you know, sir, I headed the transition team on the Federal Trade Commission for the Reagan-Bush transition team. We went into a great deal of detail researching the literature. We had a set of advisers we consulted on the matter. A member of the team had just written a book on the Federal Trade Commission and touched on a lot of these areas. And basically, the conclusion we drew was that something along the lines of these three elements would be appropriate.

I guess the major distinction is that whereas the Commission earlier in its letter said this is essentially Commission policy, I felt very strongly—and now a majority of the Commission feels at least supportive of the notion of codifying these elements into law.

Senator **Danforth**. Yes. Now, the dissenting Commissioner is Commissioner Pertschuk?

Mr. **Miller**. Yes, sir.

Senator **Danforth**. Is the basis of his dissent that he does not feel that unfairness should be codified, or that he disagrees with the definition that has been developed?

Mr. **Miller**. My understanding is that Commissioner Pertschuk believes there should be no changes in section 5 at all.

Senator **Danforth**. By no changes you mean that there should be no effort to define unfairness at all?

Mr. **Miller**. Correct.

Senator **Danforth**. Does he have any objection that you know of to the type of definition that has been put forward in this bill?

Mr. **Miller**. Sir, I cannot speak for Commissioner Pertschuk. I would wager, though, that he would say if the Congress wished to move forward on a definition of unfairness with respect to unfair acts and practices, that the three elements that I described this morning would be acceptable.

Senator **Danforth**. So there is no objection or disagreement, as you understand it, to the definition that has been suggested?

Mr. **Miller**. Well, no, sir. Of course, Commissioner Pertschuk was Chairman at the time the letter was sent to you and Senator Ford, and so, it reflects I think reasonably well his view of an appropriate policy. But he has I think a statement with respect to the reauthorization, and I think that it would be appropriate for the committee to read that.

Senator **Danforth**. Finally, Mr. Chairman, if I could just add to a point that Senator Ford made, which I think is very important with respect to an effort to define deception. It had not occurred to me that that was necessary. I had thought that deception did not cry out for definition to the extent that unfairness did. But I do think that if we are going to entertain this possibility, that between now and markup we should have a fairly extensive analysis together with examples as to the difference between deception as it has been used by the FTC and deception as you would suggest we define it in the statute. Maybe this is something that should not be done, but I do not think we should buy a pig in a poke. Thank you, Mr. Chairman.

Senator **Kasten**. I want to pick up on a point that Senator Ford was discussing. In the case of professionals, it is my opinion that some of the comprehensive licensing and regulatory programs in place at the State level for doctors, for lawyers and for others sets the FTC involvement in this area somewhat apart.

It is not clear to me why there should be layer upon layer of regulation for activities of professionals. The bill that I am developing will address this issue, perhaps somewhat more strongly than Senator Cannon's bill has. But I would just like your opinion on this layer after layer of regulation and why you feel so strongly that FTC involvement is necessary.

Mr. **Miller**. Yes, sir. I surely agree with you. One wants to avoid layer upon layer of bureaucracy. Here, though, it is not that the Federal Trade Commission is getting in to regulate the professions; it is essentially trying to make sure that the professions do not engage in ordinary restraint of trade.

We do not want them to be engaged in boycotts, in price fixing and that sort of thing. Things that are perhaps arguably, in some instances, aided and abetted by State regulation. But we would draw a distinction between anticompetitive activities which would be a violation of the antitrust laws of our Nation, and activities that are engaged in by the professions in order to improve the quality of the services they deliver and so forth.

Senator **Kasten**. But isn't that, in fact, the mandate of most of the State regulatory bodies, in one way or another? If you were testifying here as the Wisconsin commissioner or the Wisconsin head regulator of any one of those groups, and I said, "What is your job," wouldn't you use exactly the same words that you just picked?

Mr. **Miller**. Well you know, sir, it is a very sensitive problem and I have a great deal of empathy for anyone——

Senator **Kasten**. What can you do that they do not do? Or, what do you view as your mandate? One that is exclusively yours, that is not picked up by the various State regulatory bodies?

Mr. **Miller**. Under the State action doctrine as stated by the Supreme Court, you have to show essentially that first, anything violative of the U.S. antitrust laws was compelled by the State; second, that it serves a State need; and third, that that activity or conduct is supervised by the State. Then, even if it is violative of the antitrust laws, it is OK.

But, if it can be shown that their activity is not compelled by State action, then it seems to me that the Federal Trade Commission and other Federal agencies that would be concerned about such activity ought to have a chance to intervene.

Price fixing is not normally something that a State regulatory agency would be preventing. That is not the kind of conduct among the professions that they would be preventing.

But the important thing is that we have an opportunity and there is a serious need to prevent that kind of activity if the State governmental activity does not meet those three conditions; namely, compelling the activity, overseeing the activity and making it serve a State governmental purpose.

Senator **Kasten**. Last spring, the Senate Appropriations Committee included report language which essentially cautioned the commission about proposals to extend care labeling requirements to furniture, carpets and, I think, other textiles. The committee asked the Commission to give particular attention to whether a sufficient number of serious complaints had been received to justify this action to the potential impact of this rule on small business, to possible anticompetitive effects of the rule, and to the potential for increased costs created by the rule.

Can you tell me what progress, if any, the FTC has made in conducting this evaluation?

Mr. **Miller**. Well, sir, one thing that maybe not being a lawyer, instead being an economist, makes me more sensitive than a lawyer would be and that is, I have cautioned all of my staff to obey the law and other things that are included in the appropriations and the FTC Improvements Act. I have my staff looking at this information and following the law.

Now, I have been assured that we are following the dictates of the Congress in this regard. I cannot talk about the case, though, because that would sound like it may convey some prejudgment of it in one way or another.

Senator **Kasten**. We have been joined by Senator Packwood, the chairman of the full committee. Senator, do you have an opening statement or would you like to address a question to the Commissioner?

OPENING STATEMENT BY THE CHAIRMAN

The **Chairman**. Yes; Mr. Chairman I have an opening statement. I have just come from the Finance Committee where things are much more bleak than here.

Thank you, Mr. Chairman for agreeing to conduct these FTC hearings at the full committee level. I have had a long-standing interest in the FTC, as you know, and I think other members of the committee outside the Consumer Subcommittee have as well.

I would like to begin by commending you, Bob, on your recent announcement that you will oppose major reductions in the scope of the FTC antitrust authority, including reductions in the scope of the "unfair methods of competition" prohibition. Like you, I am deeply concerned about antitrust enforcement, and I think the FTC has an important role to play in enforcement at the Federal level. Not only is the FTC well suited to bring economic expertise to bear on complex antitrust issues, but the flexibility of its mandate contributes to the FTC ability to react to new problems. Its for these reasons that I am a little concerned about sections of Senator Cannon's recently introduced bill relating to "unfair methods of competition" and antitrust rulemaking. I haven't had much of a chance to study this proposal yet, but I will, and I look forward to talking about it with Howard, and about the necessity for opening this issue at this time.

Most of the testimony today and tomorrow will deal with the consumer protection side of the FTC authority. During the last authorization, I opposed some of the proposals limiting the FTC authority in the area of commercial advertising and interfering with on-going rulemakings, partly on the basis that special interest legislation was not generally in the long-run public interest, and partly due to a concern with protection of vulnerable consumers, such as children. I will review with great interest the testimony today and tomorrow with these concerns in mind.

Senator **Kasten**. Senator Ford?

Senator **Ford**. Let us pursue Senator Kasten's direction just a little bit.

How far should the Commission defer to State licensing groups?

Mr. **Miller**. Well, sir, I think really the current Supreme Court rulings on the State action defense probably draws the line about where it should be drawn.

Senator **Ford**. Where is that?

Mr. **Miller**. And that is if——

Senator **Ford**. I want you to interpret that for me. Since you are not a lawyer, I can probably understand it.

Mr. **Miller**. What it says basically is if someone is engaging in an activity that is violative of the U.S. antitrust laws, that unless they can show that a substantial State interest is at stake, then we can go after them and find them guilty of violating antitrust laws.

If, on the other hand, a substantial State interest is involved as revealed by the fact that the State regulatory agency compels them to do it, says that it serves a State plan and also supervises the activity, then it is hands off for the Federal Trade Commission.

Senator **Ford**. Well, what about quality of care issues? Should the Commission substitute their judgment for a State's judgment as it relates to quality of care?

Mr. **Miller**. I do not think it should. I do not think it should. I think States really ought to be the ones determining the mix of services to the extent that they want to be involved in that market. What I want is to make sure that when we go about doing something, we are not reducing the quality of service or changing State law in that regard.

Senator **Ford**. What about the licensing group of that particular area?

Mr. **Miller**. I know it is a close call sometimes, but if the purpose of the licensing is to keep out new competitors and it is just a blatant case of anticompetitive behavior, then I would say that really, the object of the conduct was to be anticompetitive, not to increase the quality of service. But we have to make a fine distinction there. There is no question about it.

Senator **Ford**. What about a licensing board, say, for hospitals? They are, in our State anyway, directed to try to distribute the beds instead of having an oversupply in one area and an undersupply in the other. That gets into the quality of care issue.

One of the warmest issues in several legislatures is the nursing home issue—the quality of care in nursing homes. Do you have any incentive to get into that arena at all?

Mr. **Miller**. Sir, all I can say is we will look at it very, very carefully, and I was just handed a note by one of my attorneys who says it is close to a pending case. So I really, really should not be talking too much in that specific area. It might telegraph my thoughts on that.

Senator **Ford**. Mr. Chairman, Senator Kasten, it seems to me that we have a gentleman who is beginning to talk like I want a chairman to talk and he is being restrained.

Senator **Kasten**. We have three non-lawyers here; maybe that is our problem.

Senator **Ford**. Well, my daddy always told me a little knowledge of the law is dangerous; get a good lawyer to stay with you. I guess the chairman is trying to stay with his lawyers in this case. So I will——

Mr. **Miller**. Sir, I have very good lawyers who are dedicated to——

Senator **Ford**. I understand you have over 900 over there and you can pick any of them you want.

Senator **Kasten**. Thank you, Senator.

Senator **Ford**. Wait a minute, let me just ask one other thing. I cannot let this one pass.

You indicated that you wanted your people to stay within the law.

Mr. **Miller**. Yes, sir.

Senator **Ford**. That indicated that the previous Commission overstepped its bounds.

Mr. **Miller**. Sir, I would not be so undiplomatic as to——

Senator **Ford**. Well, you said you told yours to stay within the law.

Mr. **Miller**. Yes, sir, I did.

Senator **Ford**. And we heard a lot that the previous Commission overstepped their bounds, using the theory that if they went to court and they won, they had more jurisdiction; if they lost, they had not lost any jurisdiction. So I hope you will continue to admonish your people to stay within the bounds of the law.

Senator **Kasten**. Senator Packwood?

The **Chairman**. Mr. Chairman, I wanted to say one thing. I did not hear the opening statements, and I have put mine in the record. But one of the points I hit most strongly in it was that I wanted to see no change—would not consider in the reauthorization any change that would, in any way, shape or form, diminish the Commission's antitrust authority. And I would hope that that is a subject that the Commission would not want to pursue, if they have any desire to diminish it.

Mr. **Miller**. I understand, I understand, Senator.

Senator **Ford**. There will be a bill before us that has something about antitrust in it.

The **Chairman**. Coming from you?

Senator **Ford**. No, S. 2221 introduced by Senator Cannon.

Senator **Kasten**. Chairman Miller, thank you for your testimony today. There may be additional questions from some other Senators that were here and certainly, questions from some of the Senators that were unable to attend the hearing. We would hope that you could reply to those questions within a timely period.

Thank you very much for your testimony. It is a pleasure working with you.

Mr. **Miller**. Thank you, sir, and we will be glad to answer any questions you might have.

Mr. Chairman, could I just reiterate it has been such a pleasure working with you and other members of the committee.

Senator **Kasten**. Thank you.

[The attachments referred to follow:]

FEDERAL TRADE COMMISSION,
Washington, D.C., December 17, 1980.

Hon. WENDELL H. FORD,
Chairman, Consumer Subcommittee, Committee on Commerce, Science, and Transportation, Washington, D.C.

Hon. JOHN C. DANFORTH,
Ranking Minority Member, Consumer Subcommittee, Committee on Commerce, Science, and Transportation, Washington, D.C.

DEAR SENATORS FORD AND DANFORTH: This is in response to your letter of June 13, 1980, concerning one aspect of this agency's jurisdiction over "unfair or deceptive acts or practices." You informed us that the Subcommittee was planning to hold oversight hearings on the concept of "unfairness" as it has been applied to consumer transactions. You further informed us that the views of other interested parties were solicited and compiled in a Committee Print earlier this year.[1] Your letter specifically requested the Commission's views on cases under Section 5 "not involving the content of advertising," and its views as to "whether the Commission's authority should be limited to regulating 'false or deceptive' commercial advertising." Our response addresses these and other questions related to the concept of consumer unfairness.

We are pleased to have this opportunity to discuss the future work of the agency. The subject that you have selected appears to be particularly timely. We recognize that the concept of consumer unfairness is one whose precise meaning is not immediately obvious, and also recognize that this uncertainty has been honestly troublesome for some businesses and some members of the legal profession. This result is understandable in light of the general nature of the statutory standard. At the same time, though, we believe we can respond to legtimate concerns of business and the Bar by attempting to delineate in this letter a concrete framework for future application of the Commission's unfairness authority. We are aided in this process by the cumulative decisions of this agency and the federal courts, which, in our opinion, have brought added clarity to the law. Although the administrative and judicial evolution of the consumer unfairness concept has still left some necessary flexibility in the statute, it is possible to provide a reasonable working sense of the conduct that is covered.

In response to your inquiry we have therefore undertaken a review of the decided cases and rules and have synthesized from them the most important principles of general applicability. Rather than merely reciting the law, we have attempted to provide the Committee with a concrete indication of the manner in which the Commission has enforced, and will continue to enforce, its unfairness mandate. In so doing we intend to address the concerns that have been raised about the meaning of consumer unfairness, and thereby attempt to provide a greater sense of certainty about what the Commission would regard as an unfair act or practice under Section 5.

This letter thus delineates the Commission's views of the boundaries of its consumer unfairness jurisdiction and is subscribed to by each Commissioner. In addition, we are enclosing a companion Commission statement that discusses the ways in which this body of law differs from, and supplements, the prohibition against consumer deception, and then considers and evaluates some specific criticisms that have been made of our enforcement of the law.[2] Since you have indicated a particular interest in the possible application of First Amendment principles to commercial advertising, the companion statement will include discussions relevant to that question. The companion statement is designed to respond to the key questions raised about the unfairness doctrine. However, individual Commissioners may not necessarily endorse particular arguments or particular examples of the Commission's exercise of its unfairness authority contained in the companion statement.

COMMISSION STATEMENT OF POLICY ON THE SCOPE OF THE CONSUMER UNFAIRNESS JURISDICTION

Section 5 of the FTC Act prohibits, in part, "unfair . . . acts or practices in or affecting commerce." [3] This is commonly referred to as the Commission's consumer unfairness jurisdiction. The Commission's jurisdiction over "unfair methods of competition" is not discussed in this letter.[4] Although we cannot give an exhaustive treatment of the law of consumer unfairness in this short statement, some relatively concrete conclusions can nonetheless be drawn.

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[1] Unfairness Views on Unfair Acts and Practices in Violation of the Federal Trade Commission Act (1980) (hereinafter referred to as "Committee Print").

[2] Neither this letter nor the companion statement addresses ongoing proceedings, but the Commission is prepared to discuss those matters separately at an appropriate time.

[3] The operative sentence of Section 5 reads in full as follows: "Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are declared unlawful." 15 U.S.C. 45(a)(1).

The present understanding of the unfairness standard is the result of an evolutionary process. The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loop holes for easy evasion.[5] The task of identifying unfair trade practices was therefore assigned to the Commission, subject to judicial review,[6] in the expectation that the underlying criteria would evolve and develop over time. As the Supreme Court observed as early as 1931, the ban on unfairness "belongs to that class of phrases which do not admit of precise definition, but the meaning and application of which must be arrived at by what this court elsewhere has called 'the gradual process of judicial inclusion and exclusion.'"[7]

By 1964 enough cases had been decided to enable the Commission to identify three factors that it considered when applying the prohibition against consumer unfairness. These were: (1) whether the practice injures consumers; (2) whether it violates established public policy; (3) whether it is unethical or unscrupulous.[8] These factors were later quoted with apparent approval by the Supreme Court in the 1972 case of *Sperry & Hutchinson.*[9] Since then the Commission has continued to refine the standard of unfairness in its cases and rules, and it has not reached a more detailed sense of both the definition and the limits of these criteria.[10]

CONSUMER INJURY

Unjustified consumer injury is the primary focus of the FTC Act, and the most important of the three *S&H* criteria. By itself it can be sufficient to warrant a finding of unfairness. The Commission's ability to rely on an independent criterion of consumer injury is consistent with the intent of the statute, which was to "[make] the consumer who may be injured by an unfair trade practice of equal concern before the law with the merchant injured by the unfair methods of a dishonest competitor."[11]

The independent nature of the consumer injury criterion does not mean that every consumer injury is legally "unfair," however. To justify a finding of unfairness the injury must satisfy three tests. It must be substantial; it must not be outweighed by any countervailing benefits to consumers or competition that the practice produces; and it must be an injury that consumers themselves could not reasonably have avoided.

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[4] In fulfilling its competition or antitrust mission the Commission looks to the purposes, policies, and spirit of the other antitrust laws and the FTC Act to determine whether a practice affecting competition or competitors is unfair. See, e.g., *FTC* v. *Brown Shoe Co.*, 384 U.S. 316 (1966). In making this determination the Commission is guided by the extensive legislative histories of those statutes and a considerable body of antitrust case law. The agency's jurisdiction over "deceptive acts or practices" is likewise not discussed in this letter.

[5] *See* H.R. Conf. Rep. No. 1142, 63rd Cong., 2d Sess, at 19 (1914) (If Congress "were to adopt the method of definition, it would undertake an endless task"). In 1914 the statute was phrased only in terms of "unfair methods of competiton," and the reference to "unfair acts or practices" was not added until the Wheeler-Lea Amendment in 1938. The initial language was still understood as reaching most of the conduct now characterized as consumer unfairness, however, and so the orginal legislative history remains relevant to the construction of that part of the statute.

[6] The Supreme Court has stated on many occasions that the definiton of "unfairness" is ultimately one for judicial determination. See e.g., *FTC* v. *Sperry & Huctchinson Co.* 405 U.S. 233, 249 (1972); *FTC* v. *R. F. Keppel & Bros.*, 291 U.S. 304, 314 (1934).

[7] *FTC* v. *Raladam Co.*, 283 U.S. 643, 648 (1931). See also *FTC* v. *R. F. Keppel & Bros.* 291 U.S. 304, 310 (1934) ("Neither the language nor the history of the Act suggests that Congress intended to confine the forbidden methods to fixed and unyielding categories").

[8] The Commission's actual statement of the criteria was as follows: "(1) whether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been estabished by statutes, the common law, or otherwise—whether, in other words, it is within at least the penumbra of some common-law, statutory, or other established concept of unfairness; (2) whether it is immoral, unethical, oppressive or unscrupulous; (3) whether it causes substantial industry to consumers (or competitors; (3) whether it causes substantial injury) to consumers (or competitors or other businessmen)." Statement of Basis and Purpose, Unfair or Deceptive advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8355 (1964).

[9] *FTC* v. *Sperry & Hutcinson Co.*, 405 U.S. 223, 244,-45 n.5 (1972). The Circuit Courts have concluded that this quotation reflected the Supreme Court's own views. See *Spiegel, Inc.*, v. *FTC*, 540 F. 2d 287, 293 n.8 (7th Cir. 1976); *Heater* v. *FTC*, 503 F.2d 321, 323 (9th Cir. 1974). The application of these factors to antitrust matters is behind the scope of this letter.

[10] These standards for unfairness are generally applicable to both advertising and nonadvertising cases.

[11] 83 Cong. Rec. 3255 (1938) (remarks of Senator Wheeler).

First of all, the injury must be substantial The Commission is not concerned with trival or merely speculative harms.[12] In most cases a substantial injury involves monetary harm, as when sellers coerce consumers into purchasing unwanted goods or services[13] or when consumers buy defective goods or services on credit but are unable to assert against the creditor claims or defenese arising from the transaction.[14] Unwarranted health and safety risks may also support a finding of unfairness.[15] Emotional impact and other more subjective types of harm on the other hand, will not ordinarily make a practice unfair. Thus, for example, the Commission will not seek to ban an advertisement merely because it offends the tastes or social beliefs of some viewers, as has been suggested in some of the comments.[16]

Second, the injury must not be outweighed by any offsetting consumer or competitive benefits that the sales practice also produces. Most business practices entail a mixture of economic and other costs and benefits for purchasers. A seller's failure to present complex technical data on his product may lessen a consumer's ability to choose, for example, but may also reduce the initial price he must pay for the article. The Commission is aware of these tradeoffs and will not find that a practice unfairly injures consumers unless it is injurious in its net effects.[17] The Commission also takes account of the various costs that a remedy would entail. These include not only the costs to the parties directly before the agency, but also the burdens on society in general in the form of increased paperwork, increased regulatory burdens on the flow of information, reduced incentives to innovation and capital formation, and similar matters.[18]

Finally, the injury must be one which consumers could not reasonably have avoided.[19] Normally we expect the marketplace to be self-correcting, and we rely on consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention—to govern the market. We anticipate that consumers will survey the available alternatives, choose those that are most desirable, and avoid those that are inadequate or unsatisfactory. However, it has long been recognized that certain types of sales techniques may prevent consumers from effectively making their own decisions, and that corrective action may then become necessary. Most of the Commission's unfairness matters are brought under these circumstances. They are brought, not to second-guess the wisdom of particular consumer decisions, but rather to halt some form of seller behavior that unreasonable creates or takes advantage of an obstacle to the free exercise of consumer decisionmaking.[20]

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[12] An injury may be sufficiently substantial, however, if it does a small harm to a large number of people, or if it raises a significant risk of concrete harm.

[13] See e.g., *Holland Furnace Co.* v. *FTC*, 295 F. 2d 302 (7th Cir. 1961) (seller's servicemen dismantled home furnaces and then refused to reassemble them until the consumers had agreed to buy services or replacement parts).

[14] Statement of Basis and Purpose, Preservation of Consumers' Claims and Defenses, 40 Fed. Reg. 53506, 53522-23 (1975).

[15] For an example see *Philip Morris, Inc.*, 82 F.T.C. 16 (1973) (respondent had distributed free-sample razor blades in such a way that they could come into the hands of small children) (consent agreement). Of course, if matters involving health and safety are within the primary jurisdiction of some other agency, Commission action might not be appropriate.

[16] See, e.g., comments of association of National Advertisers, Committee Print at 120. In an extreme case, however, where tangable injury could be clearly demonstrated, emotional effects might possibly be considered as the basis for a finding of unfairness. Cf. 15 U.S.C. §§ 1692 et seq. (Fair Debt Collection Practices Act) (banning, e.g. harassing late-night telephone calls).

[17] See *Pfizer, Inc.*, 81 F.T.C. 23, 62-63 n.13 (1972); Statement of Basis and Purpose, Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 43 Fed. Reg. 59614, 59636 n.95 (1978). When making this determination the Commission may refer to existing public policies for help in ascertaining the existence of consumer injury and the relative weights that should be assigned to various costs and benefits. The role of public policy in unfairness determinations will be discussed more generally below.

[18] For example, when the Commission promulgated the Holder Rule it anticipated an overall lowering of economic costs to society because the rule gave creditors the incentive to police sellers, thus increasing the likelihood that those selling defective goods or services would either improve their practices or leave the marketplace when they could not obtain financing. These benefits, in the Commission's judgment, outweighed any costs to creditors and sellers occasioned by the rule. See Statement of Basis and Purpose, Preservation of Consumers' Claims and Defenses, 40 Fed. Reg. 53506, 53522-23 (1975).

[19] In some senses any injury can be avoided—for example, by hiring independent experts to test all products in advance, or by private legal actions for damages—but these courses may be too expensive to be practicable for individual consumers to pursue.

Sellers may adopt a number of practices that unjustifiably hinder such free market decisions. Some may withhold or fail to generate critical price or performance data, for example, leaving buyers with insufficient information for informed comparisons.[21] Some may engage in overt coercion, as by dismantling a home applicance for "inspection" and refusing to reassemble it until a service contract is signed.[22] And some may exercise undue influence over highly susceptible classes of purchasers, as by promoting fraudulent "cures" to seriously ill cancer patients.[23] Each of these practices undermines an essential precondition to a free and informed consumer transaction, and, in turn, to a well-functioning market. Each of them is therefore properly banned as an unfair practice under the FTC Act.[24]

VIOLATION OF PUBLIC POLICY

The second S&H standard asks whether the conduct violates public policy as it has been established by statute, common law, industry practice, or otherwise. This criterion may be applied in two different ways. It may be used to test the validity and strength of the evidence of consumer injury, or, less often, it may be cited for a dispositive legislative or judicial determination that such injury is present.

Although public policy was listed by the S&H Court as a separate consideration, it is used most frequently by the Commission as a means of providing additional evidence on the degree of consumer injury caused by specific practices. To be sure, most Commission actions are brought to redress relatively clear-cut injuries, and those determinations are based, in large part, on objective economic analysis. As we have indicated before, the Commission believes that considerable attention should be devoted to the analysis of whether substantial net harm has occurred, not only because that is part of the unfairness test, but also because the focus on injury is the best way to ensure that the Commission acts responsibly and uses its resources wisely. Nonetheless, the Commission wishes to emphasize the importance of examining outside statutory policies and established judicial principles for assistance in helping the agency ascertain whether a particular form of conduct does in fact tend to harm consumers. Thus the agency has referred to First Amendment decisions upholding consumers' rights to receive information, for example, to confirm that restrictions on advertising tend unfairly to hinder the informed exercise of consumer choice.[25]

Conversely, statutes or other sources of public policy may affirmatively allow for a practice that the Commission tentatively views as unfair. The existence of such policies will then give the agency reason to reconsider its assessment of whether the practice is actually injurious in its net effects.[26] In other situations there may be no clearly established public policies, or the policies may even be in conflict. While that does not necessarily preclude the Commission from taking action if there is strong evidence of net consumer injury, it does underscore the desirability of carefully examining public policies in all instances.[27] In any event, whenever objective evidence of consumer injury is difficult to obtain, the need to identify and assess all relevant public policies assumes increased importance.

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[20] This emphasis on informed consumer choice has commonly been adopted in other statutes as well. See e.g., Declaration of Policy, Fair Packaging and Labeling Act, 15 U.S.C. § 1451 ("Informed consumers are essential to the fair and efficient functioning of a free market economy").

[21] See, e.g., Statement of Basis and Purpose, Labeling and Advertising of Home Insulation, 44 Fed. Reg. 50218, 50222-23 (1979); Statement of Basis and Purpose, Posting of Minimum Octane Numbers on Gasoline Dispensing Pumps, 36 Fed. Reg. 23871, 23882 (1971). See also *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.* 425 U.S. 748 (1976).

[22] See *Holland Furnace Co.* v. *FTC*, 295 F.2d 302 (7th Cir. 1961); cf. *Arthur Murray Studio, Inc.* v. *FTC*, 458 F.2d 622 (5th Cir. 1972) (emotional high-pressure sales tactics, using teams of salesmen who refused to let the customer leave the room until a contract was signed). See also Statement of Basis and Purpose, Cooling-Off Period for Door-to-Door Sales, 37 Fed. Reg. 22934, 22937-38 (1972).

[23] See e.g., *Travel King, Inc.*, 86 F.T.C. 715, 774 (1975). The practices in this case primarily involved deception, but the Commission noted the special susceptibilities of such patients as one reason for banning the ads entirely rather than relying on the remedy of fuller disclosure. The Commission recognizes that "undue influence" in advertising and promotion is difficult to define, and therefore exercises its authority here only with respect to substantial coercive-like practices and significant consumer injury.

[24] These few examples are not exhaustive, but the general direction they illustrate is clear. As the Commission stated in promulgating its Eyeglasses Rule, the inquiry should begin, at least, by asking "whether the acts or practices at issue inhibit the functioning of the competitive market and whether consumers are harmed thereby." Statement of Basis and Purposes, Advertising of Ophthalmic Goods and Services, 43 Fed. Reg. 23992, 24001 (1978).

[25] *See* Statement of Basis and Purpose, Advertising of Ophthalmic Goods and Services, 43 Fed. Reg. 23992, 24001 (1978), citing *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council*, 425 U.S. 748 (1976).

[26] Cf. Statement of Basis and Purpose, Advertising of Ophthalmic Goods and Services, supra; see also n.17 supra.

Sometimes public policy will independently support a Commission action. This occurs when the policy is so clear that it will entirely determine the question of consumer injury, so there is little need for separate analysis by the Commission. In these cases the legislature or court, in announcing the policy, has already determined that such injury does exist and thus it need not be expressly proved in each instance. An example of this approach arose in a case involving a mail-order firm.[28] There the Commission was persuaded by an analogy to the due-process clause that it was unfair for the firm to bring collection suits in a forum that was unreasonably difficult for the defendants to reach. In a similar case the Commission applied the statutory policies of the Uniform Commercial Code to require that various automobile manufacturers and their distributors refund to their customers any surplus money that was realized after they repossessed and resold their customer's cars.[29] The Commission acts on such a basis only where the public policy is suitable for administrative enforcement by this agency, however. Thus it turned down a petition for a rule to require fuller disclosure of aerosol propellants, reasoning that the subject of fluorocarbon safety was currently under study by other scientific and legislative bodies with more appropriate expertise or jurisdiction over the subject.[30]

To the extent that the Commission relies heavily on public policy to support a finding of unfairness, the policy should be clear and well-established. In other words, the policy should be declared or embodied in formal sources such as statutes, judicial decisions, or the Constitution as interpreted by the courts, rather than being ascertained from a general sense of the national values. The policy should likewise be one that is widely shared, and not the isolated decision of a single state or a single court. If these two tests are not met the policy cannot be considered as an "established" public policy for purposes of the S&H criterion. The Commission would then act only on the basis of convincing independent evidence that the practice was distorting the operation of the market and thereby causing unjustified consumer injury.

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[27] The analysis of external public policies is extremely valuable but not always definitive. The legislative history of Section 5 recognizes that new forms of unfair business practices may arise which, at the time of the Commission's involvement, have not yet been generally proscribed. See page 4, supra. Thus a review of public policies established independently of Commission action may not be conclusive in determining whether the challenged practices should be prohibited or otherwise restricted. At the same time, however, we emphasize the importance of examining public policies, since a thorough analysis can serve as an important check on the overall reasonableness of the Commission's actions.

[28] *Spiegel, Inc.* v. *FTC*, 540 F.2d 287 (7th Cir. 1976). In this case the Commission did inquire into the extent of the resulting consumer injury, but under the rationale involved it presumably need not have done so. See also *FTC* v. *R. F. Keppel & Bro.*, 291 U.S. 304 (1934) (firm had gained a marketing advantage by selling goods through a lottery technique that violated state gambling policies); cf. *Simeon Management Corp.*, 87 F.T.C. 1184, 1231 (1976), *affd*, 579 F.2d 1137 (9th Cir. 1978) (firm advertised weight-loss program that used a drug which could not itself be advertised under FDA regulations) (alternative ground). Since these public-policy cases are based on legislative determinations, rather than on a judgment within the Commission's area of special economic expertise, it is appropriate that they can reach a relatively wider range of consumer injuries than just those associated with impaired consumer choice.

[29] A surplus occurs when a repossessed car is resold for more than the amount owed by the debtor plus the expenses of repossession and resale. The law of 49 states requires that creditors refund surpluses when they occur, but if creditors systematically refuse to honor this obligation, consumers have no practical way to discover that they have been deprived of money to which they are entitled. See *Ford Motor Co.*, 94 F.T.C. 564, 618 (1979) appeal pending, Nos. 79-7649 and 79-7654 (9th Cir.); *Ford Motor Co.*, 93 F.T.C. 402 (1979) (consent decree); *General Motors Corp.*, D. 9074 (Feb., 1980) (consent decree). By these latter two consent agreements the Commission, because of its unfairness jurisdiction, has been able to secure more than $2 million for consumers allegedly deprived of surpluses to which they were entitled.

[30] See Letter from John F. Dugan, Acting Secretary, to Action on Smoking and Health (January 13, 1977). See also Letter from Charles A. Tobin, Secretary, to Prof. Page and Mr. Young (September 17, 1973) (denying petition to exercise § 6(b) subpoena powers to obtain consumer complaint information from cosmetic firms and then to transmit the data to FDA for that agency's enforcement purposes).

UNETHICAL OR UNSCRUPULOUS CONDUCT

Finally, the third S&H standard asks whether the conduct was immoral, unethical, oppressive, or unscrupulous. This test was presumably included in order to be sure of reaching all the purposes of the underlying statute, which forbids "unfair" acts or practices. It would therefore allow the Commission to reach conduct that violates generally recognized standards of business ethics. The test has proven, however, to be largely duplicative. Conduct that is truly unethical or unscrupulous will almost always injure consumers or violate public policy as well. The Commission has therefore never relied on the third element of S&H as an independent basis for a finding of unfairness, and it will act in the future only on the basis of the first two.

We hope this letter has given you the information that you require. Please do not hesitate to call if we can be of any further assistance.

With best regards,

Michael Pertschuk, *Chairman.*
Paul Rand Dixon, *Commissioner.*
David A. Clanton, *Commissioner.*
Robert Pitofsky, *Commissioner.*
Patricia P. Bailey, *Commissioner.*

Enclosure.

Companion Statement on the Commission's Consumer Unfairness Jurisdiction

This statement is intended to supplement the Commission's letter on the consumer unfairness jurisdiction. It will discuss two additional subjects. The first is the manner in which the unfairness jurisdiction relates to and complements the ban against deceptive practices, and the second is a consideration of certain specific criticisms that have been made of the enforcement of the unfairness jurisdiction.[1]

I. THE NEED FOR THE PROHIBITION OF UNFAIR ACTS OR PRACTICES

The Commission's unfairness jurisdiction has become an important part of its ability to protect consumers against certain abusive practices. The unfairness standard supplements, rather than duplicates, other aspects of the FTC Act. The various components of the statute form an intergrated whole, allowing the Commission to promote the diverse benefits of a free and open economy. Thus the ban on unfair competition prevents exclusionary or anticompetitive behavior and helps preserve a full variety of marketplace options for consumers to choose among; the ban on deception helps ensure that consumers will not make that choice on the basis of misleading information; and the ban on unfair practices ensures that the choice is not distorted by coercion, the withholding of important information, or similar practices. Safeguards at all three levels are needed to ensure that substantial consumer injury is adequately addressed.

There are many ways in which consumer decisions may be distorted or coerced without resort to clear, outright deception. For this reason the Commission has challenged many practices, including most of those discussed below, as both deceptive and unfair. Elimination of the Commission's unfairness jurisdiction and sole reliance on a deception standard in its stead[2] would at best create ambiguity about the status of such practices and at worst permit significant abuses that the law now clearly prevents. The drawbacks of eliminating the Commission's unfairness jurisdiction are illustrated by the Eyeglasses Rule, which involved several different restraints on consumer choice.[3] The Commission found that many optometrists refused to give customers written copies of their lens prescriptions, so that consumers who received eye examinations from one practitioner were prevented from shopping to buy their eyeglasses from less expensive providers. These restraints were not deceptive, but they often prevented consumers from buying eyeglasses at the lowest possible price. Their combined effect was to inflate artificially the cost of eye care, a burden which fell most heavily on the poor and the elderly. A statute which did not prohibit unfair acts or practices would have made it difficult for the Commission to prevent this injury.

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[1] As before, this statement does not address the Commission's jurisdiction over unfair methods of competition.

[2] Some suggestions to this effect have appeared in the Committee Print. See, e.g., Comments of General Mills, Inc. (Committee Print at p. 22); Comments of Sears, Roebuck & Co. (Committee Print at p. 139); Comments of the American Retail Federation (Committee Print at p. 156).

[3] Trade Regulation Rule, Advertising of Ophthalmic Goods and Services, 43 Fed. Reg. 23992 (1978). Portions of the rule were later remanded for the Commission to determine whether sellers had changed their practices in light of recent Supreme Court decisions. *American Optometric Ass'n* v. *FTC*, 626 F. 2d 896 (D.C. Cir. 1980).

Buyers are sometimes overtly coerced. Some sellers have, for example, pressured consumers into a distraught state of mind, even physically preventing them from leaving the room during the sales presentation, in order to coerce a sale.[4] In other instances, door-to-door salesmen have refused to leave customers' homes until they purchased expensive goods or services.[5] Both of these practices were so coercive that they tended to curtail the free exercise of consumer choice.

Sometimes consumer unfairness is found even without coercion or denials of product information. A striking example arose in the early 1970's when a company began promoting razor blades in a way that risked serious injury to small children. Free samples of the blades were included indiscriminately in advertising supplements to home-delivered newspapers, without any protective packaging that would keep children who found them from injuring themselves. The Commission was able to use its unfairness jurisdiction to negotiate a consent decree barring this unsafe marketing technique.[6] A statute allowing the Commission to move only against deception might have left it less able to protect children against the practice.

Most of the Commission's consumer unfairness actions have historically been directed against techniques other than commercial advertising, since the most serious abuses in advertising have often involved some form of deception and thus could be challenged directly under that portion of the statute. However, the Commission has also encountered injurious advertising practices which ought to be prohibited, and that could most readily be characterized as unfair. Thus the Commission has used its authority over unfair acts and practices to negotiate consent decrees barring advertisements which needlessly depicted young children engaged in unsafe or illegal behavior, thereby creating a danger that other children would be led to imitate what they saw.[7] Also, the Commission has required advertisements to disclose product information that was necessary for consumers to compare the efficiency of competing brands of home insulation[8] and the octane levels of competing brands of gasoline.[9] The absence of this information tended seriously to undercut the ability of consumers to make rational product choices, causing substantial consumer injury.

As we have noted before, certain aspects of these practices might be reached under a deception theory, but the issue is unclear and it seems difficult to rely exclusively on deception to reach all instances of coercion, overreaching and inadequate product information disclosure. It might, of course, be theoretically possible to correct these abuses individually, by passing a series of specifically tailored prohibitions without resort to a general statutory ban on unfair acts and practices. This approach has serious drawbacks, however; indeed, it was considered and rejected by Congress nearly seventy years ago when it first enacted Section 5. As the Senate Commerce Committee reasoned then, "The Committee gave careful consideration to the question as to whether it would attempt to define the many and variable unfair practices which prevail in commerce and to forbid their continuance or whether it would, by a general declaration condemning unfair practices, leave it to the commission to determine what practices were unfair. It concluded that the latter course would be better, for the reason, as stated by one of the representatives of the Illinois Manufacturers' Association, that there were too many unfair practices to define, and after writing 20 of them into law it would be quite possible to invent others." [10]

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[4] *Arthur Murray Studio, Inc.*, 78 F.T.C. 401, 439–41 (1971), aff'd, 458 F. 2d 622 (5th Cir. 1972).

[5] See Statement of Basis and Purpose, Cooling-Off Period for Door-to-Door Sales, 37 Fed. Reg. 22934 (1972). Other aspects of this rule, of course, involved deceptive practices. For a litigated case involving the rule see *New Rapids Carpet Center, Inc.*, 90 F.T.C. 64, 119–20 (1977).

[6] *Philip Morris, Inc.*, 82 F.T.C. 16 (1973).

[7] E.g., *AMF, Inc.*, C-3011 (1980) (bicycle advertisement showing children riding bicycles in violation of proper highway safety rules); *Mego International*, 92 F.T.C 186 (1978) (children playing with electrical appliances near water and without adult supervision); *Uncle Ben's, Inc.*, 89 F.T.C 131 (1977) (advertisement showing young children cooking on a gas range without adult supervisions), *General Foods Corp.*, 86 F.T.C. 831 (1975) (natural-food advocate eating wild nuts and berries).

[8] Trade Regulation Rule, Labeling and Advertising of Home Insulation, 44 Fed. Reg. 50218 (1979).

[9] Trade Regulation Rule, Posting of Minimum Octane Numbers on Gasoline Dispensing Pumps, 36 Fed. Reg. 23871 (1971). The Commission found that it would be more effective to desclose the information at the point of sale than in media advertising, but the principle is the same.

[10] S. Rep. No. 597, 63d Cong., 2d Sess. 13 (1914). See also H.R. Rep. No. 1142, 63d Cong., 2d Sess. 19 (1914) ("It is also practically impossible to define unfair practices so that the definition will fit business of every sort in every part of this country. Whether competition is unfair or not generally depends upon the surrounding circumstances of the particular case.")

In short, the language of "unfairness" has been an integral part of the FTC Act from its beginnings. It represents a considered judgment on the part of Congress and the courts that the Commission can interpret a reasonably flexible statute with sufficient specificity to protect consumers in the context of a continually evolving marketplace. The unfairness standard, in conjunction with the rule against deception, is necessary to enable the Commission to address the full range of business practices that result in substantial injury to consumers and distortion of the marketplace.

II. SPECIFIC CRITICISMS OF THE CONSUMER UNFAIRNESS AUTHORITY

Notwithstanding the general development of the FTC's consumer unfairness authority as described above, some specific questions have been raised about its application to particular circumstances. A number of these have been collected in the Committee print, "Views on Unfair Acts and Practices in Violation of the Federal Trade Commission Act." There appear to be three major questions. These express concern that the unfairness authority: (1) is an overbroad delegation of discretionary authority which allows the Commission to restrict practices that cause no consumer injury; (2) fails to give adequate notice of what conduct will be considered unfair; and (3) may violate the First Amendment when applied to commercial speech. Each of these points will be considered in turn.

Agency discretion and consumer injury

The discussion in our letter on the limits to the Commission's unfairness jurisdiction will, we hope, allay concerns that the agency might find practices to be unfair in the absence of consumer injury, or that its unfairness jurisdiction leaves too much to its discretion. As stated therein, the presence of unjustified consumer injury—whether shown by objective evidence, by clear public policy, or both—is essential to a determination that particular conduct is unfair. Similarly, the discussion should indicate that the bounds of the Commission's discretion under its unfairness jurisdiction have been clarified and limited.

In addition to the definable limits on unfairness as described in the Commission's letter, there are also external procedural checks which ensure that the agency does not overstep the bounds of intended congressional delegation. Industry-wide rules are subject to formal congressional review under the terms of recent amendments to the Federal Trade Commission Act.[11] Further, all Commission rules and orders are subject to judicial review.[12] Professor Kenneth Culp Davis, a leading authority on administrative law, has concluded that safeguards of this type provide a more meaningful check on agency discretion than would actions to prescribe more specific standards.[13] Congressional and judicial review of agency determinations of unfairness will, moreover, contribute to the continual process of more precisely defining the proper scope of the Commission's unfairness jurisdiction.

Adequacy of notice

A second concern is that the statutory term "unfair" is too imprecise to give business adequate notice of what conduct will be considered improper. To the extent that this concern rests on questions about the scope of agency discretion, these issues have been addressed above. To the extent that this concern also rests upon perceptions of procedural unfairness, the Commission would like to bring to the committee's attention procedural protections that currently exist in both its adjudicative and rulemaking proceedings.

Under the Federal Trade Commission Act, businesses cannot be subjected to sanctions for engaging in an unfair practice until the practice has been defined with specificity in a full-dress adjudication or rulemaking.[14] If, in an adjudication, a firm is found to have engaged in a newly identified unfair act or practice, civil penalties are not assessed; rather, the remedies are limited to preventing the firm from engaging in the same or related practices in the future,[15] and, in appropriate cases, to providing relief for injured parties. Only if the order is violated may penalties then be assessed.[16] There are also some special provisions for immediate consumer redress, but these apply only to conduct that "a reasonable man would have known under the circumstances was dishonest or fraudulent," and that determination must be made in federal court.[17]

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[11] See FTC Improvements Act of 1980, Pub. L. 96–252, §21.

[12] See, e.g., *FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233, 249, (1972); *FTC* v. *R. F. Keppel & Bro.*, 291 U.S. 304, 314 (1934).

[13] See K. Davis. Administrative Law Treatise, §2.00–3, at 47 (1970 Supp.). For this reason statutes that imply a similar degree of discretion in other agencies have been regularly upheld. See, e.g., *National Broadcasting Co.* v. *United States*, 319 U.S. 190 (1943) (upholding FCC's reliance on its power to license broadcasting stations in "the public interest, convenience, or necessity" as authority for issuing regulations concerning contractual relations between broadcasters and networks); *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) (upholding the Federal Power Commission's area rate fixing regulations under the statutory power to determine whether independent producers of natural gas have rates that are "just and reasonable"). While these other agencies may have a more specific subject matter under their jurisdiction, within that jurisdiction they have a degree of discretion that is not unlike the FTC's.

[14] See 15 U.S.C. §§45(b), 57a.

The situation in rulemaking is similar. The Commission's rulemaking authority was clarified and its powers to enforce its rules through the assessment of civil penalties were expanded in 1975, with the passage of the Magnuson Moss Federal Trade Commission Improvements Act. However, in granting the Commission this new authority, Congress also imposed procedural requirements on the rulemaking process that significantly exceed the protections that the Administrative Procedures Act affords participants in the proceedings of other agencies.[18] For example, participants in Magnuson Moss rulemakings have the right to conduct cross examination on disputed issues of material fact, to present oral testimony to the Commission, and to offer rebuttal evidence at various stages of the proceeding.[19] More recently Congress provided additional procedural protections to participants in FTC rulemakings. For example, the Commission is required to publish an "advance notice of proposed rulemaking" to obtain public input in the initial stages of a Commission inquiry, even before any particular rule provisions are proposed.[20] In addition, the Commission must issue a preliminary regulatory analysis weighing projected costs and benefits of any proposed rule and a final regulatory analysis when promulgating a final rule.[21] Finally, firms that are unsure whether certain activities are legally unfair are at all times invited to seek advisory opinions from the staff.

First amendment considerations

A third concern is that the First Amendment forbids the regulation of "unfair" but nondeceptive advertisements since these are essentially a form of protected commercial speech.[22] The Commission agrees that the First Amendment imposes stringent limitations upon the extent to which the government may regulate nondeceptive commercial speech, but further believes that the First Amendment does not entirely preclude such regulation.[23] Far from constituting a reason for eliminating the Commission's unfairness jurisdiction as it pertains to advertising, the First Amendment protections accorded commercial speech constitute a strong argument against the need for legislative modification of the unfairness mandate, since they already ensure that the unfairness clause may be applied to advertising only under limited circumstances.

Supreme Court decisions on commercial speech have made clear that deceptive commercial speech, and commercial speech that advocates an illegal activity, are entitled to no constitutional protections.[24] By contrast, commercial speech that neither deceives consumers nor advocates illegal conduct is entitled to substantial constitutional protection.[25] The extent of such protection was articulated by the Supreme Court in the recent case of *Central Hudson Gas and Electric Corp.* v. *Public Service Comm'n.*[26] At issue in that case was a state regulation prohibiting public utilities from advertising to promote the increased use of electricity. The majority found that such commercial speech was entitled to some constitutional protection because it was not misleading and did not relate to unlawful activity. However, if then determined that such speech could still be regulated by the government consistently with the First Amendment provided that three criteria were met. First, the government must assert a substantial interest to be served by its regulation of commercial speech. Second, the restriction must directly advance the stated governmental interest. Finally, the restriction may not be more extensive than necessary.[27] The Supreme Court has thus generally described the boundaries of the government's authority to limit commercial speech that does not mislead or encourage illegal activity.

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[15] 15 U.S.C. §45(b). See *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 394–95 (1965); *FTC* v. *National Lead, 352 U.S. 419, 429 (1957); FTC* v. *Ruberaid Co.*, 343 U.S. 470, 473 (1952); *Joseph Siegel Co.* v. *FTC*, 327 U.S. 608, 612–13 (1946).

[16] See 15 U.S.C. §45(1).

[17] See 15 U.S.C. §576(a).

[18] See 5 U.S.C. § 551 et seq.

[19] See 15 U.S.C. § 57a(c).

[20] See FTC Improvements Act of 1980, Pub. L. 96–252 (May 28, 1980) § 8, 15 U.S.C. § 57a(b).

[21] Id. at § 15, 15 U.S.C. § 57b–3.

[22] This objection pertains to the Commission's unfairness authority only as it relates to advertising. The Commission's principal past uses of unfairness have occurred with respect to sales practices that did not involve commercial speech.

[23] *Central Hudson Gas and Electric Corp.* v. *Public Service Comm'n.* 100 S.Ct. 2343, 2351 (1980).

[24] *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 771–72 (1976); *Central Hudson supra*, 100 S.Ct. at 2351.

[25] The Supreme Court has, however, upheld prophylactic measures designed to prevent serious risks of deception or coercion. In *Ohralik* v. *Ohio State Bar Ass'n.*, 436 U.S. 447, 462 (1978), for example, the Court upheld a rule against in-person solicitation of clients by lawyers, suggesting that such rules could be valid even without specific findings that deception or coercion had actually occurred. See also *Friedman* v. *Rogers*, 99 S.Ct. 887, 896 (1979) (regulating conduct found to create "a significant possibility" of deception).

[26] 100 S.Ct. 2343 (1980).

In the past the Commission has made sparing use of its unfairness authority to regulate commercial speech.[28] To the extent that it may need to exercise such authority in the future, it will do so in conformity with the standards established in *Central Hudson.* Moreover, the Commission recognizes that commercial speech questions involve a developing area of constitutional law. For example, *Central Hudson* did not define precisely when a governmental interest will be deemed substantial. Furthermore, the case involved state regulations and thus the considerations applied to the Commission's mandate to eliminate unfair practices may not be precisely the same.[29] The Commission will therefore proceed with caution as the courts continue to refine the standards for governmental regulation of nondeceptive commercial speech.

III. CONCLUSION

In short, three things may be said about the Commission's consumer unfairness jurisdiction. First, the commission has sought to construe its jurisdiction in limited, specific, and market-oriented terms. Second, the Commission may be less able to reach many instances of significant consumer harm if its jurisdiction is limited to "deception." Third, the Commission has attempted to define its unfairness jurisdiction with sufficient particularity to answer criticisms that the law is excessively uncertain or is invoked in circumstances that threaten freedom of speech.

By direction of the Commission.

CAROL M. THOMAS, *Secretary.*

Federal Trade Commission,
Washington, D.C., March 5, 1982.

Hon. BOB PACKWOOD,
Chairman, Committee on Commerce, Science and Transportation, U.S. Senate, Washington, D.C.

Hon. BOB KASTEN,
Chairman, Subcommittee on Consumer, Committee on Commerce, Science and Transportation, U.S. Senate, Washington, D.C.

DEAR CHAIRMAN PACKWOOD AND CHAIRMAN KASTEN: This is in response to your letter of February 24, 1982, in which you ask for the Commission's views with respect to our jurisdiction over state-regulated professionals and unfair acts or practices as currently defined in Section 5 of the Federal Trade Commission Act. As you know, these issues have been raised by the recent introduction of S. 1984, a bill that could substantially restrict the Commission's authority in these and other areas. Thus, we welcome this opportunity to state our views on these matters and, where appropriate, shall refer to the pertinent provisions of S. 1984. In the near future, we shall respond to Chairman Packwood's request for a complete comment on S. 1984.

In brief, the Commission opposes any provision of law that grants, or would grant, state-regulated professionals (and associations of professionals) immunity from law enforcement that others do not enjoy. With respect to our jurisdiction over unfair acts or practices, we believe that a more precise statutory standard is appropriate.[1]

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[27] 100 S.Ct. at 2351.

[28] Indeed, in the Eyeglasses Rule the Commission used its unfairness authority to free commercial advertising from unjustified restrictions.

[29] Even apart from constitutional considerations, the Commission's need to consider consumer injury and public policy before determining whether a practice is unfair means that it has less freedom to take many of the regulatory actions that are open to the states.

[1] Commissioner Pertschuk dissents on this point and wishes to add the following comment:

Continued

Such a clarification, based on the statement on consumer unfairness issued by the Commission on December 17, 1980, would clarify the legal bounds of acceptable behavior and alleviate any uncertainty about the Commission's exercise of its authority under the provisions of the Federal Trade Commission Act. In our view, these two issues are interrelated. While we believe there is ample statutory authority for the Commission's activities concerning the professions, we also believe that it is entirely proper for Congress to specify more clearly the scope of our consumer unfairness jurisdiction based on our 1980 Policy Statement. Under these circumstances, a special exemption for professionals, which would restrict the Commission's ability to foster competition and promote consumer welfare in these significant sectors of the national economy, would be particularly unwise.

THE PROFESSIONALS AND CONSUMER WELFARE

The Federal Trade Commission has, over the last several years, examined certain practices of professionals and their organizations. Our activities do not derive from any desire to regulate the professionals but rather from a basic concern that some restrictions on competition among professionals increase consumer costs without producing countervailing benefits. Our objective, in both our competition and our consumer protection activities, is to enhance the ability of informed consumers to act as ultimate regulators of the market.

Professional services are an increasingly important sector of the economy, and the efficiency of this industry is of prime importance to consumers. The service sector has been the most rapidly growing component of the economy for many years. Health care, the major focus of recent Commission interest, is the largest single component of the service sector. In 1980 alone, Americans spent over $247 billion on health care services or 9.4 percent of the Gross National Product.

In light of these facts, the Commission believes that effective consumer protection and the fostering of competition cannot exclude professional services. The Commission's activities in this area have not sought to interfere either with legitimate self-regulation or with the authority of the states to assure the quality of services to their citizens. Instead, the record shows that the Commission has concerned itself only with specific barriers to competition and restrictions that demonstrably harm consumers.

Acting under its current statutory authority, the Commission has pursued three specific types of matters concerning professionals. First, the Commission has brought traditional antitrust cases involving allegations of price fixing, boycotts, and other private agreements or conspiracies to restrain or eliminate competition. In the *American Medical Association* case now before the Supreme Court, the Commission found that the AMA had prohibited almost all forms of truthful advertising by physicians and had unnecessarily restricted the ability of physicians to contract with hospitals and other organizations not controlled by physicians. Accordingly, the Commission entered an order to prevent repetition of these anticompetitive practices, but the order expressly permits the AMA to adopt and enforce reasonable ethical guidelines to prevent false or deceptive advertising and oppressive forms of solictation. See *American Medical Ass'n*, 94 F.T.C. 701 (1978), aff'd, 638 F.2d 443 (2d Cir. 1980), cert. granted, 49 U.S.L.W 3946 (U.S. June 22, 1981) (No. 80-1690) (argued Jan. 11, 1982). Other antitrust matters have involved alleged boycotts against health maintenance organizations, alleged conspiracies to obstruct cost-containment programs, alleged boycotts by doctors against a hospital emergency room because the hospital was planning to retain its own doctor, and alleged boycotts by doctors against a state medicaid program that sought to contain health care costs.

Second, the Commission has sought to prevent false or deceptive advertising, and other fraudulent practices, by certain professionals. For example, the Commission proceeded against advertisements for synthetic hair implants in which there was

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While I agree with most of the Commission's letter, I dissent from the view that the authority of the Commission to proscribe "unfair . . . acts or practices" should be restated in complex statutory language. The December, 1980 Policy Statement of the Commission reviewed at length the history of Commission and court decisions construing Congressional intent for this authority since 1914 and demonstrated that a careful framework for Commission decisionmaking in this area has been achieved. To incorporate the principles of the Policy Statement into legislation will principally benefit the lawyers of our country by providing tempting opportunities for lengthy (and costly) battles over interpretation. If it is Congress' desire to do so, however, I support the principles of the Policy Statement and agree with my fellow Commissioners that it should serve as the basis for a statutory definition. An attempt to begin anew the task of writing a definition would take us into a legal quagmire from which another half century of court opinions might be needed to extricate us.

reason to believe that the medical risks involved in the implant process had not been adequately disclosed. *Terrance D. Lesko, M.D.,* Docket No. C-3031 (July 28, 1980); *FTC* v. *Kazdin,* Civil No. 79-1857 (N.D. Ohio, June 30, 1980) (order granting permanent injunction).

Third, the Commission has examined the effects of restrictions by state and professional associations on certain business aspects of professional services. These activities have been designed primarily to free the market from burdensome, unnecessary regulation and not to add a new layer of federal regulation. For example, the Commission's one promulgated rule sought to eliminate restrictions on advertising the prices of eyeglasses and eye examinations. In another area of great importance to consumers, the Commission developed a model state statute regarding drug product anti-substitution laws.

In exercising its current antitrust and consumer protection authority regarding the professions, the Commission has closed investigations and declined to initiate a rulemaking in areas in which the Commission concluded that action would be inappropriate. For example, the Commission concluded that antitrust concerns about the alleged control of some medical prepayment plans by physician groups ought to be addressed on a case-by-case basis rather than through rulemakings. In another area, the Commission terminated an investigation of advertising prohibitions by a veterinary association because the group voluntarily amended certain of the restrictions.

The proposed exemption in S. 1984 would effectively foreclose all Commission activities involving any state-regulated professional. State-licensed and regulated professionals and their associations would be exempted from all Commission activities, including studies, reports to the Congress and the public, investigations, law enforcement, and rulemaking conducted under the FTC Act. Because the bill does not define "professions", its intended scope is somewhat unclear, but Senator McClure, one of its principal sponsors, has stated that the term includes "lawyers, engineers, physicians, dentists, optometrists, architects, accountants, veterinarians, and the like." 127 Cong. Rec. at S. 15686 (Dec. 16, 1981). Given the imprecise nature of the bill's defining language, virtually any occupation would be able to argue that it too was exempt from FTC authority.

Another subsection of S. 1984 would, in effect, prohibit the Commission from bringing complaints under Section 5 against professionals and against professional associations, as long as the state licensing authority regulated the profession in some manner. Under this provision, any state regulation of any aspect of a profession results in a total exemption for all the activities of all members of the profession. For example, solely on the basis of a state regulatory scheme consisting of licensure and regulations to prevent negligent behavior, members of the profession would be exempted from Section 5's prohibitions against price fixing and fraud.

Other provisions would remove the authority that section 6 of the FTC Act now provides for the Commission to investigate state-regulated professions, their individual members, and their state and national professional associations. It would limit the Commission's ability to study the economic effects of state and federal regulations concerning the professions, to participate in the proceedings of other agencies, or to assist the courts through amicus curiae briefs. It would also remove any authority under the FTC Act for the promulgation of rules that affect the professions or their members.

The consequences of these proposals are most disturbing. In sum, they would prohibit the Commission from taking any action against, or even investigating, classic collusive activities, such as price fixing and group boycotts, in the professions. The bill would also exempt state-regulated professions from challenges under the FTC Act to false advertising and fraudulent marketing practices, including practices in or affecting interstate commerce that might not be susceptible to effective state regulation. It would immunize the activities of individual professionals and groups of professionals on the sole ground that they were licensed and regulated in some manner by the state. The legislation might also render unenforceable the Commission's order in the *American Medical Association* case, which is awaiting decision in the Supreme Court, and cast doubt on our ability to enforce outstanding consent decrees and orders litigated before the Commission and upheld by the courts.

Although the Department of Justice could still bring criminal and civil actions and private parties could institute treble damage actions challenging alleged violations of the Sherman Act and the other antitrust laws, there would be no general federal remedy for deceptive practices involving the professions. Moreover, the Commission could not apply its economic expertise to the investigation and adjudication of claims that certain professional activities were excessively anticompetitive. We believe that an agency equipped with economic expertise is especially suited to the analysis of the effects of public and private regulations concerning the professions, and that an agency whose authority is limited to the issuance of prospective, nonpunitive orders to cease and desist is especially able to adjudicate the sensitive issues raised by antitrust challenges involving the professions.

To repeat, we do not believe there is any sound justification for exempting "professionals" from the traditional investigational and law enforcement jurisdiction to which virtually all other business enterprises are subject. Even with a restricted definition, such an exemption suggests that a special class of occupations is beyond the traditional rules of law. If professionals are free to enforce restrictions that result in barriers to free consumer choice and artificially inflated prices, immune from the safeguards of the FTC Act, the evidence is strong that consumers will suffer direct and tangible injury.

Another feature of S. 1984 would disrupt the ability of the Commission to promote the functioning of the free market with respect to both the professions and the entire industrial sector of the economy. That would appear to result through an extremely broad exemption related to activities "in conformance with" state law.

That operative phrase is potentially boundless and would surely invite unnecessary litigation. For example, the phrase might refer to conduct mandated by state law, conduct expressly sanctioned by state law, conduct regulated by state law, or conduct that simply does not violate state law. At its broadest reading, this provision would immunize against FTC action a practice illegal under federal law merely because a state had not itself legislated against the practice. Indeed, the FTC would be prohibited from so much as gathering information about such a practice. Such a result would be entirely inconsistent with federal responsibility for the efficient functioning of a national economy.

Even under a narrower reading, this provision would adversely affect the public interest because it would make the FTC Act much narrower than the Sherman Act and thus restrict the Commission's ability to prohibit essentially private restraints of trade merely because there is some tangential government involvement. Under the Sherman Act, conduct that constitutes "state action" is not subject to antitrust scrutiny, but private parties cannot use the existence of some government involvement as a shield to protect private restraints of trade. Under this bill, state regulation not intended to protect anticompetitive conduct would provide such a shield.

Finally, this provision would absolutely preclude Commission preemption of any state law. The only instance in which the Commission promulgated a rule challenging state laws regulating the professions was the 1978 Eyeglasses Rule, which eliminated state prohibitions on the truthful advertising of eyeglasses and eye examinations. During the 18 months that the rule was fully in effect, competition in the vision care market increased, and prices declined dramatically for eyeglasses and contact lenses. For example, industry observers cited increased competition in the contact lens market stimulated by the Eyeglasses Rule as the primary reason for a 28 percent reduction in wholesale prices for contact lenses. (Business Week, Nov. 5, 1979, at 125.) The Eyeglasses Rule was subsequently remanded by the Court of Appeals for the Commission to reconsider the need for a preemptive rule in light of changed legal circumstances, namely Supreme Court decisions on the First Amendment's protection of commercial speech.

We are, of course, cognizant of the importance of federalism and the need to consider carefully the values associated with state autonomy. Undeniably, preemption is a significant power and must be viewed as a remedy of last resort. At a minimum, certain conditions should be present before exercising this power. They include: the costs to consumers of the state law should be clearly shown; the alleged benefits of the state law should be shown to be minimal or absent; there should be evidence that the states are not acting on their own to change the laws; and the benefits of competition among the states should be minimal or absent.

Although we believe that the Commission has acted carefully with respect to the professions and state regulation, we recognize that there is concern over some past interpretations of our authority in some other areas, such as the scope of our "unfair . . . acts or practices" authority. As we discuss below, we believe that the answer to these concerns is to define that phrase, not to exclude entire segments of the economy, such as the professions, from jurisdiction or to eliminate helpful remedial tools. In our view, the approach of S. 1984 simply suggests that certain persons are beyond the rules by which other members of our society are governed.

THE COMMISSION'S JURISDICTION OVER "UNFAIR * * * ACTS OR PRACTICES"

By letter dated December 17, 1980, the Commission stated its general views concerning the definition of an unfair act or practice. The Commission felt that one of the most crucial elements in finding an act or practice to be unfair was that consumers be injured. The Commission listed three basic elements for evaluating consumer injury: (1) the injury must be substantial; (2) the injury must not be outweighed by any countervailing benefits to consumers or competition produced by the practice; and (3) the injury must be an injury that consumers could not reasonably have avoided.

As a federal body, the Commission believes its concerns should be with substantial injuries; its resources should not be used for trivial or speculative harm. As a general proposition, substantial injury involves economic or monetary harm and does not cover subjective examples of harm such as emotional distress or offenses to taste or social belief.

In addition, the injury should not be outweighed by consumer or competitive benefits resulting from the challenged practice. Clearly, most business practices involve an economic and social mixture of costs and benefits; hence, unless a particular practice has the net effect of being injurious, the Commission should refrain from finding it unfair. In reaching its decision, the Commission should take into account costs related to a prospective remedy, including but not limited to direct cost to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and capital formation and like matters.

Finally, an unfair act or practice must be one which consumers could not reasonably have avoided. The Commission should not be involved in rectifying the unfortunate choice of a particular consumer decision. It should confine its activities to curb behavior that takes unfair advantage of consumers' inadequate knowledge in reaching a decision or inability to protect themselves from such behavior.

Additionally, although it is not a necessary element of the definition of unfairness, the Commission also looks to other established public policies in an effort to determine whether a particular practice is unfair. As the Commission indicated in its 1980 Policy Statement, reference to other public policies may provide additional evidence of consumer injury or, conversely, it may influence the Commission to reconsider its tentative view that a practice is injurious in its net effects and, therefore, unfair. A thorough analysis of such policies "can serve as an important check on the overall reasonableness of the Commission's action." Dec. 17, 1980 Policy Statement at page 10, note 27.

As a matter of practice, the Commission considers the foregoing factors in reaching any decision concerning an act or practice alleged to be unfair. That being so, it is appropriate and logical to include these three elements in a statutory definition of "unfairness". The codification of its acknowledged practices will not only aid the Commission but also consumers and sellers to understand the bounds of acceptable behavior without diminishing the ability of the Commission to police the marketplace.

In recommending the elements of a definition of consumer unfairness, the Commission recognizes the appropriateness of having Congress provide as much guidance as feasible to administrative agencies. Since the Commission has recently spelled out the criteria it will utilize in defining unfairness, codification of those criteria can help to provide specific guidance for those regulated as well as the regulator.

As to the element pertaining to the weighing of benefits and costs, however, the Commission believes there is an associated problem to consider, namely the risk that the analysis might unnecessarily complicate and delay an investigation or an ultimate litigation. For this reason, the Commission believes that a highly quantitative benefit/cost analysis may not be appropriate in each and every individual case, and that in some cases a far more subjective analysis would be the reasonable approach. We believe any legislative history of a refined definition of unfairness should reflect this view.

We appreciate this opportunity to comment on two of the central questions being addressed by the Congress during the reauthorization process.

By direction of the Commission.

James C. Miller III, *Chairman.*

[The following information was subsequently received for the record:]

Federal Trade Commission,
Washington, D.C., April 23, 1982.

Hon. Bob Packwood,
Chairman, Committee on Commerce, Science and Transportation, U.S. Senate, Washington, D.C.

Dear Mr. Chairman: As indicated in our letter to you of March 5, 1982, we promised to respond to your request for a complete comment on S. 1984, introduced in the Senate by Senator McClure on December 16, 1981. We are happy to do so.

The bill consists of nine sections. Sections 2 through 8 amend or repeal various provisions of the Federal Trade Commission Act. The operative sections provide exemptions for state-regulated professions and their associatons (Sec. 2); forbid law enforcement and rulemaking proceedings directed to, or the collection of information concerning, activities "in conformance with" state law (Sec. 3); require the Commission to pay the costs of subpoena compliance (Sec. 4); revoke the Commission's authority to issue subpoenas and instead require the Commission to apply to a district court for such process (Sec. 5); define "unfair methods of competition" and "unfair or deceptive acts or practices" to mean acts that cause "substantial consumer injury that outweighs the benefits derived from such act[s]" (Sec. 6); eliminate administrative cease and desist proceedings and substitute court proceedings (Sec. 7); and repeal the program for financing intervention in rulemaking by interested groups (Sec. 8). The bill would become effective immediately upon approval (Sec. 9).

As stated in our previous letter, we believe that enactment of any special exemption for state-regulated professionals and for conduct "in conformance with" state law would be unwise. We do believe it would be appropriate to redefine the standard for liability under Section 5 of the Federal Trade Commission Act, but we prefer the changes indicated in our recent testimony to the changes incorporated in the bill. We oppose the provisions in the proposed legislation that would revoke the Commission's authority to issue subpoenas in law enforcement proceedings, require the Commission to reimburse the costs of compliance with subpoenas, and repeal the Commission's authority to conduct administrative adjudications of complaints charging unfair methods of competition and unfair or deceptive acts or practices. In our view, these provisions would severely hamper the Commission's ability to protect consumers and promote competition.

EXEMPTIONS FOR PROFESSIONALS AND FOR CONDUCT "IN CONFORMANCE WITH" STATE LAW

In our March 5 letter, we commented extensively on those portions of the bill that would create a broad exemption for state-regulated professionals and for activities conducted "in conformance with" applicable state law. A copy of that letter is enclosed for your review. We wish to note in addition that although the exemption for actions taken "in conformance with" state law appears to be prompted by concern about Commission actions involving the professions, the exemption is not so limited. Moreover, this exemption would not only prohibit law enforcement and rulemaking proceedings but would also preclude studies and reports on the impact of regulation upon competition and consumer welfare. Reports to the Congress, the public and the state concerning the economic effects of government regulation are fully compatible with our federal system, as are challenges to unnecessarily anticompetitive regulations under the limited circumstances described at p. 7 of the March 5 letter.

SUBPOENAS AND DATA-GATHERING

Section 5 of the bill would repeal the Commission's authority to issue administrative subpoenas. Instead, the Commission would be required to proceed by requesting the attendance and testimony of witnesses and the production of documents. If the respondent declined the request, the Commission could then apply for the issuance of a subpoena to a district court "within the jurisdiction of which [the] inquiry [was being] carried on." The district court that issued the subpoena would apparently also decide subsequent motions to quash and to limit it.

Administrative agencies commonly have the power to issue their own compulsory process and, indeed, Congress has incorporated the Commission's statutory authority to issue subpoenas into statutes granting other agencies compulsory process. This bill would reject considerable past experience, commencing from when the Interstate Commerce Commission was first granted subpoena authority in 1889, and substitute for it a lengthy procedure for the Commission's investigatory mission.

Allowing an administrative tribunal to issue subpoenas and dispose of motions to modify or quash them permits resolutions of disputes concerning the subpoenas before there is any need to resort to the judiciary. The instant proposal, however, would place the entire burden on the courts. Moreover, the bill would seem to interpose unnecessary delay and impose upon the Commission and the taxpayers the cost of going to court over each and every subpoena.

Before imposing time-consuming judicial procedures on the Commission's efforts to obtain the information necessary to effective law enforcement, we urge the Congress to study the impact of the protections contained in the FTC Improvements Act of 1980, particularly wilth respect to civil investigative demands. If Congress wishes to apply additional safeguards to the exercise of the Commission's investigatory powers, we believe an appropriate step would be to extend to antitrust investigations the civil investigative demand procedures now applicable only to investigations of unfair or deceptive acts or practices.

Section 4 of the bill would amend Section 9 of the FTC Act to provide for reimbursement of "reasonable costs including attorneys' fees of [any] person, partnership, or corporation complying with [an] information request."

Under present legal requirements, agencies generally must reimburse a complying party only for costs that "exceed * * * that which the party ought reasonably be made to shoulder." *SEC* v. *Arthur Young & Co.* 584 F.2d 1018, 1033 (D.C. Cir. 1978, *cert denied,* 439 U.S. 1071 (1979). The courts have held that "[t]here is a continuing general duty to respond to governmental process; in consequence, subpoenaed parties can legitimately be required to absorb reasonable expenses of compliance with administrative subpoenas." Id.

This provision would shift to the federal budget the costs of complying with requests for information needed in law enforcement investigations and, like Section 5 of the bill, would single out this agency by imposing a unique restriction upon its ability to fulfill its law enforcement mission.

Moreover, litigation of claims for attorneys' fees is particularly difficult, both for the parties to the litigation and for the courts. The Fifth Circuit has noted the "difficult job of the trial judge in cases of this kind * * *. The trial judge is necessarily called upon to question the time, expertise, and professional work of a lawyer which is always difficult and sometimes distasteful." *Johnson* v. *Georgia Highway Express, Inc.,* 488 F.2d 714, 720 (5th Cir. 1974). Parties generally bear their own litigation costs. Because there is no apparent justification for shifting litigation costs to the government and to the taxpayers, as well as imposing additional burdens upon the federal courts, we oppose this provision.

DEFINITION OF "UNFAIR METHODS OF COMPETITION" AND "UNFAIR OR DECEPTIVE ACTS OR PRACTICES"

Section 6 of the bill would amend Section 5 (a)(1) of the FTC Act by specifying that: "For purposes of this Act, an unfair method of competition or an unfair or deceptive act or practice shall be an act which causes substantial consumer injury that outweighs the benefits derived from such act."

In our March 5 letter, we stated our view as to how Section 5 might appropriately be amended. On March 18, I testified on behalf of the Commission (Commissioner Pertschuk, dissenting) before the Consumer Subcommittee of your committee. My testimony, a copy of which is enclosed, addresses this issue and sets forth the Commission's position, as well as my own personal position, in greater detail.

TRANSFER OF JURISDICTION TO THE DISTRICT COURTS

Section 7 of the bill would repeal the Commission's authority to conduct administrative adjudications of complaints challenging unfair methods of competition and unfair or deceptive acts or practices. Instead, the proposal would confer jurisdiction to grant injunctive relief for violations of Section 5 on the district courts. A conforming amendment to Section 5(1) of the FTC Act would apparently render unenforceable cease and desist orders now on the books.

The intent of the 1914 Congress that created the Federal Trade Commission was to establish an expert body that would identify anticompetitive and anticonsumer trade practices, develop a coherent body of case law, and devise, through the medium of the cease-and-desist order, remedies that would both prevent repetition of the condemned practices and ensure that the effects of such practices were undone. As stated by one court.

"The enforcement scheme embodied in the Federal Trade Commission Act stresses the Commission's role in providing certainty and specificity to the broad proscriptions of the Act. The FTC, as a quasi-judicial tribunal, has the ability to provide for the centralized and orderly development of precedent applying the regulatory statute to a diversity of fact situations. [*Holloway* v. *Bristol-Myers Corp.*, 485 F.2d 986, 998 (D.C. Cir. 1973).]"

Instead, the bill would disperse the decisional process among more than 500 federal district judges and impose upon them the responsibility for resolving what are often complex issues of economics and public policy. The disadvantages of this approach were cogently pointed out more than forty years ago at page 14 of the final report of the Attorney General's Committee on Adminstrative Procedure (1941) where it observed that—

"[t] he 94 Federal district and territorial courts are structurally incapable of the same uniformity in the application of law as a single centralized agency."

In addition, today these courts have enough litigation and do not need any additional burden.

A leading commentator on administrative law and procedure has observed that—

"[t] he very identifying badge of the modern adminstrative agency is the combination in the same hand of the judicial power to adjudicate cases and the legislative power of rulemaking, along with the executive power to enfore, to investigate, to initiate, and to prosecute. [K. Davis, *Administrative Law Treatise*, Vol. 1 at 71 (2d ed. 1978).]"

Administrative orders to cease and desist are subject to judicial review of the entire record of the Commission's actions under the strict substantial evidence standard, so that the courts of appeals and the Supreme Court have the ultimate responsibility for determining that the law has been violated (see, e.g., *FTC* v. *Sperry and Hutchinson Co.*, 405 U.S. 233, 249 (1972); *FTC* v. *R. F. Keppel & Bro.*, 291 U.S. 304, 314 (1934)), and the courts have uniformly rejected claims that the combination of adjudicatory and prosecutorial functions is intrinsically unfair. See, e.g., *Withrow* v. *Larkin*, 421 U.S. 35, 47 (1975); *FTC* v. *Cinderella Career and Finishing School, Inc.*, 404 F. 2d 1308, 1315 (D.C. Cir. 1968).

PUBLIC PARTICIPATION FUNDING

Section 8 would repeal the Commission's authority to provide compensation to participants in rulemaking proceedings conducted under Section 18 of the FTC Act. Currently, Commisssioner Clanton and I favor repeal of this authorization. Commissioners Pertschuk and Bailey wish the authorization to be extended.

We appreciate this opportunity to present our comments on this bill.

By direction of the Commission.

JAMES C. MILLER III, *Chairman.*

QUESTIONS OF THE CHAIRMAN AND THE ANSWERS THERETO

Question 1. With respect to deception aimed at vulnerable groups, such as children, why do you feel that only "knowing" deception should be actionable? Especially since the cease and desist order remedy works prospectively, why shouldn't even accidental deceptions of children or other groups be prohibited?

Answer. I do not feel that only "knowing" deception aimed at vulnerable groups should be actionable. When a deceptive practice is aimed at a vulnerable group, it would not be necessary to show that the advertiser "knew or should have known" that the ad was likely to mislead. A reasonable interpretation of the ad depends on the circumstances, including the age, sophistication, and vulnerability of the ad's intended audience. An ad that is aimed at a vulnerable group should be evaluated against the reasonableness of that group.

Moreover, the Commission can also protect vulnerable groups under an unfairness theory, as outlined in our December 1980 letter to Senators Ford and Danforth.

I have attached a memorandum that analyzes the proposed standard in more detail. (Attachment No. 1.)

Question 2. When will the Commission's evaluation of its Line of Business program be completed? What is your present view about the value of the program?

Answer. A draft of the cost-benefit analysis concerning the current and potential alternative data collection formats for the LB program is scheduled to be completed by the Bureau of Economics staff and delivered to the Commission by July 1, 1982. Because the study is in progress, I do not wish to give any definite views on the value of the program at this time. Let me say, however, that I intend to give careful consideration to the results of the cost-benefit analysis as well as to any public comments that are received in response to the recent Federal Register notice. Only after all of this information is in can the required weighing of the issues be made. I certainly intend to keep Congress informed as the Commission goes about arriving at its decision on the LB program.

Question 3. Some of the witnesses at the hearing recommended repeal of Section 5(m)(1)(B) of the FTC Act. How has this authority been used by the FTC since it was enacted in 1975? Please be as specific as possible.

Answer. In utilizing Section 5(m)(1)(B) the Federal Trade Commission has adopted a two-part approach. It has prepared short summaries of FTC determinations in several dozen areas of trade practices (e.g., bait and switch advertising, billing for unordered merchandise, ect.) and served them, along with the full texts of the underlying FTC decisions and a copy of Section 5(m)(1)(B), on business firms. Approximately 3,000 of these summaries (called "synopses") have been served since section 5(m)(1)(B) was enacted in 1975. Sometimes these synopses are served on a particular segment of an industry in an effort to inform the companies of the Commission's determinatons regarding specified practices. At other times the synopsis is served on one or two firms suspected of violating the law to inform them that if they continue to engage in such practices they could be subject to Commission action.

Frequently, once a synopsis has been served, the FTC staff will follow-up with an investigation to determine whether the firm is complying with the law as set forth in the synopsis. If violations are found to be continuing, the FTC will recommend to the Justice Department that an action for monetary civil penalties be brought in U.S. District Court. Since 1975 approximately 35 such actions have been brought. Almost all involved consent judgments negotiated by the FTC staff and then referred to Justice at the same time as the complaint. Six have gone through some litigation before settlement was reached. Four cases are still in litigation.

Attached is a list of the particular Section 5(m)(1)(B) program, including a short description of each. (Attachment 2.)

Question 4. Please summarize the public cases now pending at the FTC involving charges of resale price maintenance, indicating which of these have been initiated since October 1981. Also, please provide a summary of the public statements (such as speeches, testimony, or interviews) made by any of the Commissioners or any of the Bureau Directors, Deputy Directors or Assistant Directors on the subject of resale price maintenance since October 1. Has the Commission's enforcement policy with respect to resale price maintenance changed?

Answer. The following are the only resale price maintenance cases pending at the Federal Trade Commission which are currently public:

1. *Russell Stover Candies, Inc.*, Docket No. 9140. (Complaint issued July 1, 1980, Initial Decision March 26, 1981, Appeal Argued July 6, 1981.)
2. *Onkyo U.S.A. Corp.*, File No. 801 0117. (Consent agreement provisionally accepted September 16, 1981; 60 day public comment period ended November 24, 1981; final agreement pending before Commission as of April 2, 1982.)
3. *Germaine Monteil Cosmetiques Corp.*, File No. 801 0800 (Consent agreement provisionally accepted January 19, 1982; 60 day public comment period ended March 26, 1982.)

In addition to these public resale price maintenance cases, there are currently approximately 16 nonpublic investigations underway which involve allegations of resale price maintenance. No resale price maintenance investigations initiated since October 1981 are now public. It is unlikely that any investigation commenced since that date would have reached the stage at which such cases become public (typically upon provisional acceptance by the Commission of a consent decree), since the investigation and negotiation necessary to reach that point typically take longer than the six months which have elapsed since then.

* * * * * * *

The subject of resale price maintenance was raised at my first press conference on October 26, 1981.

Question. Mr. Chairman, how do you feel about resale price maintenance?

Answer. Resale price maintenance . . . is a complicated matter . . . not one that you can give a simple answer to. I have doubts about certain vertical activities that the Commission has been engaged in in the past. We need to look at resale price maintenance and see whether there are anti-competitive consequences of the kinds of things that are proposed but you have to look at this on a case by case basis. But, generally, I've been critical of the amounts of resources that the commisson has devoted to that issue in the past.

An article in the Bureau of National Affairs' Daily Report for Executives stated: "Miller opposed applying a per se standard to resale price maintenance situations "to the extent I could legally". He said resale price maintenance "can be a procompetitive tool," especially where a new firm wants to enter a market and provide extensive service on its product. 19 Daily Report for Executives C-1 (January 28, 1982)."

Most recently, on April 2, 1982, in a speech before the Antitrust Section of the American Bar Association, I stated:

"The principles on which we base our Robinson-Patman enforcement also guide our Resale Price Maintenance enforcement. As with Robinson-Patman, there are clearly situations in which Resale Price Maintenance is anti-competitive, particularly where it facilitates collusion among manufacturers or dealers. But in other cases—for example, where point of sale service is a means of entry—where point of sale service is a means of entry—Resale Price Maintenance can be procompetitive. We plan to scrutinize those cases very carefully and will issue complaints and accept consent orders only where they are likely to increase consumer welfare."

Commissioner Clanton addressed the Fifteenth Annual New England Antitrust Conference on November 13, 1981 and stated:

"Of even greater interest at present is the treatment to be afforded resale price maintenance, or vertical price fixing. Because of Congressional repeal of the fair trade laws and recent Supreme Court reaffirmations, the law seems quite clear the Resale Price Maintenance is per se illegal. The status of the law, however, has not dampened the debate over whether per se treatment should be continued.

"It is argued the Resale Price Maintenance serves many of the same purposes for which non-price distributional retraints are imposed, such as inducing dealers to provide more pre-sale or post-sale services. In fact, it has been suggested by one commentator that Resale Price Maintenance is less restrictive than an exclusive territorial arrangement because under Resale Price Maintenance only one form of intrabrand competition is eliminated.[1] Others, however, contend that Resale Price Maintenance is more conducive to price stability because it facilitates price monitoring and coordination among competitors.[2] And, those who oppose relaxation of the per se standard further argue that manufacturers still have access to less restrictive alternatives for achieving their marketing goals."

I do not propose to resolve the debate today. But I will offer my own observations. There are undoubtedly rational business justifications for Resale Price Maintenance that have little or nothing to do with horizontal price fixing or price coordination. Yet, it also seems quite plausible that vertical price fixing, especially when it is in fairly widespread use, can facilitate pricing interdependence. For example, the presence of multi-line retailers can produce opportunities for monitoring and coordination, since the cooperation of only a few retailers may be required to keep manufacturers abreast of their competitors' pricing strategies.

Nevertheless, while further inquiry is highly desirable, I do not believe the Commission should abandon the per se standard at this time. I take this position for several reasons. First, I believe RPM has a reasonably clear anti-competitive potential, although the potential may not be great in all circumstances. Second, no satisfactory test has yet been devised for readily distinguishing between good and bad RPM. Third, the law is relatively clear, and I am reluctant to endorse a significant change without having a fairly clear consensus about either the need for change or the suitability of an alternative test. Fourth, experience suggests that there are means other than RPM available to manufacturers for inducing retailers to provide adequate pre- or post-sale service, although I realize that not all of these alternatives are equally desirable.

I am not a believer in following precedent blindly, without regard to the soundness of the underlying assumptions. But, in the RPM area, I do not feel we have a sufficient basis yet to justify a dramatic departure in our treatment of this practice. To the extent that market conditions (outside the per se context) should receive some consideration in these cases, I would suggest that they be considered, at least initially, as policy factors in deciding which cases to pursue.

Since the Federal Trade Commission is composed of five different Commissioners with independent views, it is frequently difficult to make categorical statements concerning "Commission policy." However, my statements quoted above make clear that my view is that the FTC should pursue resale price maintenance cases where the practices complained of are anticompetitive and where FTC action will increase consumer welfare.

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[1] Posner, The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality, 48 U.Ch.L.Rev. 6 (1981).

[2] See, e.g., L. Sullivan, Handbook of the Law of Antitrust 379 (1977); P. Areeda, Antitrust Analysis 504 (2d ed. 1974).

QUESTIONS OF SENATOR GORTON AND THE ANSWERS THERETO

Question 1. The Commission's December 1980 Statement synthesized the legal development of the unfairness doctrine since 1938.

Has the Commission initiated any actions since that time that do not conform with the standards articulated in its December 1980 Statement?

(If not) Why is a statutory change necessary?

Are there any examples you can cite of final Commission actions, which were upheld by the courts and which would not have satisfied the standards in the 1980 policy statement?

Answer. The Commission's 1980 policy statement synthesized the preexisting law of consumer protection. It was intended to clarify matters rather than to break new ground. As a result, I am not aware of any final Commission actions, upheld by the courts, which would not have satisfied the standards of the policy statement, although a few relatively minor instances of that type might possibly be found. Similarly, all final Commission actions taken since the issuance of the policy statement have been in conformity with that document. Past proposals that the Commission has ultimately declined to adopt have nonetheless imposed substantial costs on those who would have been affected.

Nevertheless, it would be highly useful for Congress to pass additional legislation codifying these standards. That would serve a number of purposes. It would offer more precise guidance to the Commission staff, which has sometimes pursued theories broader than those ultimately endorsed by the Commission; it would offer reassurance to the business community; and it would ensure that the standards of the policy statement are retained and are not abandoned by a future Commission.

Question 2. If the standard "causes substantial injury and is not outweighed by countervailing benefits" is incorporated into the FTC Act, would the agency be compelled to conduct a cost/benefit analysis for every case before bringing a suit alleging unfair practices?

What would such an analysis involve?

Would it involve quantification of costs and benefits in dollars and cents?

What would happen if no precise figures were available to quantify benefits because they could only be projected to occur in the future and would be difficult to measure in the present?

Should the federal courts review the sufficiency of any cost/benefit analysis prepared by the agency? (If yes) What standards of review would a court use?

How would this requirement relate to the cost/benefit provisions of S. 1080?

Answer. One standard we have proposed for inclusion in the FTC Act is that the injury to consumers "should not be outweighed by consumer or competitive benefits resulting from the challenged practice." This standard sets out a limited cost/benefit analysis that the Commission must perform. That analysis, like other elements in its decision, should be subject to judicial review. Since the relevant factors in the balance will sometimes be complex and intangible, however, the court should not insist on a precise quantification of matters that may not lend themselves to that treatment.

Cost-benefit analysis does not require a formal quantification of every variable. It does require that the agency think systematically about the effects of its proposed actions, and that it consider all such effects. In a definition of unfairness, this requirement would mean that the agency must set forth the beneficial and adverse effects of its proposed actions, and have sufficient evidence to conclude that benefits exceed costs before it acts. In some instances, a qualitative assessment will suffice. In other cases, a more elaborate analysis would be necessary. In close cases, such an analysis will enable the agency to reach better decisions.

Question 3. In its March 5, 1980, letter to Senators Kasten and Packwood, the Commission said that the substantial injury standard should apply to unfairness when the injury is one that consumers could not reasonably have avoided.

What does "acting reasonably" mean in this context? How much responsibility does it place on the consumer to research and investigate every aspect of a commercial transaction?

Are there any examples of cases in which the Commission actually found a practice to be unfair where consumers, acting reasonably, could have avoided the injury?

Answer. The third element in the consumer unfairness test asks whether the injury "is one that consumers could not reasonably have avoided." This standard is intended to focus the Commission on seller conduct that impairs the free exercise of consumer choice.

The standard is primarily intended to protect the exercise of consumer choice. The FTC Act is a market oriented statute. It seeks to free the market from distortions such as deception or antitrust violations, and then relies upon consumers to protect their own interests by making free choices among the products that are before them. On occasion, however, sellers may adopt methods that impair the exercise of this consumer choice, and thus prevent consumers from protecting themselves in this manner. Such conduct is "unfair" within the meaning of Section 5. Examples include sales techniques that physically coerce a consumer into making a purchase (e.g., destroying an old item so that he must buy a new one), or that subject him to extreme high-pressure sales pitches, or that withhold certain pieces of essential information that he needs in order to make a knowledgeable decision.

I am aware of no final decision in which a practice was found to be unfair even though consumers, acting reasonably, could have avoided the injury. Past proposals, however, have ranged far more broadly, and have imposed significant costs on all involved.

Question 4. You have stated that your proposal to redefine deception represents your personal views. Do the other Commissioners disagree with your position? Why do they disagree? I would like to ask that the other Commissioners submit their views on this subject for the record.

Answer. The three other Commissioners do not support my proposal to redefine deception. As you know, Commissioner Pertschuk sent the Subcommittee a separate statement the day of the hearing. That statement set forth his views on deception. In letters to Commissioners Clanton and Bailey, Senator Gorton requested they submit statements on deception, for the record. I understand they have forwarded their responses to him.

Question 5. Your proposal has three elements (1) adopting of a "materiality" standard from the common law; (2) an exemption for statements of opinion; and (3) a limitation of deception to situations where "reasonable" consumers are likely to be deceived, except in cases affecting "vulnerable" groups where a company "knew or should have known" a practice was deceptive.

Answer. I am answering each of the subparts of Question 5; however, I have attached a memo prepared by the Director of the Bureau of Consumer Protection that addresses these issues in detail. (See Attachment No. 2.)

Question 6. What, in your view, is the common law meaning of "materiality" in a deception context?

Answer. In the common law, a misrepresentation has to be "material" in order to be actionable. This means that the plaintiff must show he justifiably relied on the misrepresentation. The test seeks to identify facts to which a reasonable consumer might attach importance in making the purchasing decision. (See Memo, note 43 and accompanying text.)

Question 7. How does that differ from the way the courts have already interpreted Section 5—i.e., to require a finding that the misrepresentation is material to a purchasing decision? *FTC* v. *Colgate-Palmolive,* 380 U.S. 374, 392 (1965).

Answer. Although the courts have paid lip-service to the need to find a misrepresentation is material, in fact they have allowed the Commission, upon little or no evidence, to infer that a misrepresentation is important in the purchasing decision. Thus, unlike a common law, proof of likelihood of consumer injury is not necessary to a Section 5 action.

Question 8. The courts permit the Commission to infer that a deception statement affects marketplace decision; would the changes you propose have the effect of disallowing that inference and requiring instead that the Commission conduct surveys to determine actual consumer behavior? How would such a change affect the agency's ability to police false advertising? How would you conduct such a survey in the case of a national TV ad? What are examples of bad cases the Commission has brought that would be precluded by your new standard? That is, what precisely is that the Commission had done which you seek to prevent it from doing by this proposed definition?

Answer. In appropriate cases, the proposed changes would still allow for an inference that a deceptive statement affects marketplace decisions. The Commission would not always have to conduct surveys to determine actual consumer behavior. As mentioned in the attached memo on deception, in most instances, a logical inference that injury is likely would suffice (Memo, p. 22). In those instances where the likelihood of consumer injury was unclear, the Commission would need some extrinsic evidence to proceed. For instance, it might need a survey that compared the price of the product with and without a specific feature that was falsely described in an ad. Or, it might develop survey evidence on the importance of the attribute or feature to the consumer.

A consumer survey for an investigation of a national TV ad, like a national print ad, would require that a sample of consumers be drawn. We could seek consumers who had never seen the ad, or consumers who had seen the ad, or some of each subgroup. We could also expose a sample to the ad under investigation and then ask them questions about the ad and the product. Methods for testing consumer interpretations of ads are well-established in theory and in practices. I do not envision that the proposed changes would detract from the agency's ability to police false advertising.

I have attached a list of cases that I relied upon in my testimony. Most of these cases were brought during the 1970's. The list includes some earlier cases, because they indicate the wide discretion available to the Commission in its consideration of the deceptiveness of a particular claim.

I have several specific objections to the current and past interpretation by the Commission of deception. First, the Commission has not always interpreted ads as would reasonable consumers. Thus, it has sometimes found that ads conveyed meanings that only unreasonable consumers would reach. Second, the Commission mistakenly has pursued what were called "opinion" claims at common law. I believe it should not pursue subjective claims, obviously exaggerated or puffing claims, or correctly stated descriptions of expert opinions. (See the attached memo, p.18). Third, it has not always found that the deception is likely to cause substantial consumer injury, and has pursued cases where injury is extremely unlikely. Indeed, I believe some Commission decisions have actually harmed consumers (Memo, pp. 27-28). Fourth, too often the Commission has relied on its own expertise to interpret the meaning of ads, and to find consumer injury. Sometimes the ad meaning will be clear and the likelihood of consumer injury can be inferred. In close cases, however, the Commission should not rely on its alleged expertise, but on extrinsic evidence.

Question 9. As for the distinction between "fact" and "opinion" claims and a statutory change that would exempt the latter, doesn't the law already recognize that "mere puffery" is not actionable by the FTC? If so, why is a change necessary? What are exampels of bad cases the FTC has brought that would be prohibited by this revised standard?

Answer. The opinion-fact distinction is one grounded in the common law. At common law, statements of opinion generally were not actionable, although misstatements of fact were. Statements that are clearly exaggerated, or puffing in nature, should not be actionable, because reasonable consumers would not in fact rely on them. The common law definition of opinion also exempted clearly subjective claims, such as those regarding taste, appearance, or smell.

The Commission definition of "puffery" is more limited than at common law, because the Commission is not limited to reasonable interpretations of advertising claims. Those problems are exacerbated by the Commission's reliance on its own expertise to determine what an ad means, and whether it is mere puffery. As the attached list of case indicates, the Commission has sometimes pursued opinion cases in the past.

Question 10. You suggest that the FTC Act should only cover deception of "reasonable" consumers, unless the agency can show the company "knew or should have known" the act or practive would deceive a vulnerable group. What is a vulnerable group? Why should an intent requirement apply to a prospective remedy like civil penalties where it already applies? Would the change in effect require the agency to prove the company had actual notice that a practice was deceptive? What would "actual notice" mean in a practice? What are example of bad cases the Commission has brought that would be prohibited by the new standard?

Answer. The proposed standard would cover reasonable consumers, as well as reasonable or ordinary members of a vulnerable group. For instance, an ad that is only relevant to a vulnerable group might be evaluated against the reasonableness of that group. Although no precise definition of a vulnerable group would be necessary, a "vulnerable" group is simply any group where the standard of reasonableness that we would expect of normal adults would not apply. Children are an obvious example.

The "knew" or "should have known" standard allows the Commission to challenge an ad directed to a larger audience which misleads certain members within that larger audience. Thus, the Commission could still challenge the ad if it can show that the advertiser knew or should have known that the ad would mislead some members of the audience group. Under this alternative standard, the Commission would not have to show that the company had "actual notice" that the practice was deceptive. The Commission need not prove that the advertiser intended the consequences of a particular communication; rather, it is enough to show that the advertiser should have realized the risk that those consequences could follow. This standard is needed in these cases, because when the Commission acts against claims that are only deceptive to a small minority of the audience, it inevitably restricts truthful and useful information to the majority.

The proposed changes are not meant to impede the Commission's role in protecting vulnerable groups. Instead, they are directed at ensuring that the Commission pursue only those claims that reasonable consumers, including reasonable vulnerable consumers, would draw.

Question 11. How would your proposals affect state enforcement of little FTC Acts?

Answer. The effect of an amendment to the FTC Act on state enforcement of little FTC Acts turns on the answers to two questions: (1) To what extent must state administrators and state courts, in applying their own consumer protection laws, follow the standards set out is Section 5 of the FTC Act and in decisions interpreting Section 5? (2) What bearing would an amendment to the FTC Act made after enactment of the state statutes and federal case law applying that amendment have on enforcement of the state statutes?

These questions would have to be resolved by the state courts. Moreover, because the language of the state statutes varies, it is difficult to generalize about the impact of amendments to the federal statute. What follows is an analysis of the state little FTC Acts and case law construing them. All fifty states now have some form of little FTC Act.

Many state statutes reflect an intention by the legislatures that guidance in the construction of their acts should be found in interpretations given to Section 5(a)(1) of the FTC Act, 15 U.S.C. § 45(a)(1). Two statutes provide that state courts "may" be guided by interpretations Section 5 of the FTC Act.[1] Nine provide that "consideration" or "due consideration and great weight," "should" or "shall" be given to interpretations of Section 5.[2] Nine statutes declare a legislative intent that the state courts "shall" or "will" be "guided," are to "be guided," or "to the extent possible will be guided by" interpretations of Section 5 or of Federal law.[3] Two state acts declare a legislative intent that the statute "be interpreted and construed consistently with" interpretations of the FTC Act,[4] two delare a legislative purpose to make state regulation of consumer sales practices consistent with federal Law,[5] and eight statutes provide that state rules and regulations "shall not be inconsistent" with rules and decisions interpreting Section 5.[6] These provisions allow state courts to decline to follow federal decisions that they believe are not proper guides to the meaning of their statutes. See, e.g., *State ex rel. Kidwell* v. *Master Distributors, Inc.*, 101 Idaho 447, 615 P.2d 116, 122 (1980); *State* v. *Reader's Digest Ass'n*, 81 Wash. 259, 501 P.2d 290, 301 (1972) (en banc), appeal dismissed, 411 U.S. 945 (1973) ("when appropriate we will consider the pertinent federal court interpretations of section 5 of the FTC Act. But in each case the question of what constitutes an 'unfair method of competition' or an 'unfair or deceptive act or practice' under [the Washington statute] * * * is for us, rather than the federal courts, to determine."). Moreover, these interpretive clauses only refer to those portions of the state statutes that use the unfair or deceptive language of Section 5(a)(1) of the FTC Act and they do not bear on provisions in many of the state laws prohibiting certain specific acts and practices.

Thirty-five statutes include provisions that exempt conduct (or certain kinds of conduct, such as advertising) that is "required or permitted" by state or federal law, that is "authorized under laws or regulations," or that is "specifically" "authorized" or "permitted" by federal or state law.[7] Some of these statutes use different lan-

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[1] Ariz. Rev. Stat. Ann. § 44-1522; N.H. Rev. Stat. Ann. § 358-A:13.

[2] 1981 Ala. Acts 81-355, § 6; Alaska Stat. § 45.50.545; Fla. Stat. Ann. § 501.204; Idaho Code § 48-604(1); Ill. Ann. Stat. ch 121 1/2, § 262; Md. Com. Law Code Ann. § 13-105; Mont. Code Ann. § 85-403(1); Ohio Rev. Code Ann. § 1345.02(C), § 1345.05(B) (2); R.I. Gen Laws § 6-13.1-3.

[3] Conn. Gen. Stat. Ann. § 42-110(b); Me. Rev. Stat. Ann. tit. 5, § 207; Mass. Gen. Laws Ann. ch. 93A, § 2(b); N.M. Stat. Ann. § 57-12-4; S.C. Code Ann. § 39-5-2(b); Tex. Bus. & Com. Code Ann § 17.46 (c)(1); Vt. Stat. Ann. tit. 9, § 2453(b); Wash. Rev. Code Ann. § 19.86.920; W. Va. Code § 46A-6-101.

[4] Ga. Code Ann. § 106-1201(c); Tenn. Code Ann. § 47-18-115.

[5] Fla. Stat. Ann. § 501.202; Utah Code Ann. § 13-11-2.

[6] Conn. Gen. Stat. Ann. § 42-110b(c); Fla. Stat. Ann. § 501.205; Idaho Code § 48-604(2); Me. Rev. Stat. Ann. tit. 5, § 207; Mass. Gen Laws Ann. ch. 93A, § 2(c); Mont. Code Ann. § 85-403(2); Vt. Stat. Ann. tit. 9, § 2453(c); W. Va. Code § 46A-6-103.

[7] 1981 Ala. Acts 81-355, § 4(c); Alaska Stat. § 45.50.481; Ariz. Rev. Stat. Ann. § 44-1523; Ark. Stat. Ann. § 70-913(a), (c); Colo. Rev. Stat. § 6-1-106; Conn. Gen. Ann. § 42-110c(a); Del. Code Ann. tit. 6, § 2513(b), 2534(a); Fla. Stat. Ann. § 501.204; Ga. Code Ann. § 106-1206(a); Haw. Rev. Stat. § 481A-5(a)(1); Idaho Code § 48-605(1); Ill. Ann. Stat. ch. 121½. § 270b, § 314(1); Ind. Code Ann. § 24-5-0.5-b; Iowa Code Ann. § 714.16; Ky. Rev. Stat. Ann. § 367.176(2); La. Rev. Stat. Ann. § 1406(4); Mass. Gen. Laws Ann. ch. 93A, § 3(a); Mo. Ann. Stat. § 407.020(1); Mont. Code Ann.

Continued

guage, including language exempting conduct the complies with the rules and regulations of, and the statutes administered by, the Commission.[8] Although the interpretation of these exemptions in light of any amendments to the FTC Act would also have to be resolved by the state courts, we do not believe that these provisions, particularly those exempting conduct that is "specifically authorized" by federal law, can be interpreted to immunize conduct simply because it is not prohibited by Section 5. See *Garland* v. *Mobil Oil Corp.*, 340 F. Supp. 1095, 1099 (N.D. Ill. 1972) (practices not within exemption for "conduct in compliance with the orders or rules of or a statute administered by a Federal * * * agency" because not "mandated" by federal law); *State* v. *Reader's Digest Ass'n*, *supra*, 501 p. 2d at 303 (exemption for actions "otherwise permitted, prohibited or regulated under laws administered by * * * any regulatory body or officer acting under statutory authority of * * * the United States" inapplicable to laws administered by FTC).

Twenty-seven state statutes say nothing about the weight to be given interpretations of the FTC Act[9] and 12 say nothing about either the weight to be given interpretations of the FTC Act or the effect of a person's compliance with federal law.[10] Some state courts have followed federal case law interpreting Section 5, see, *e.g.*, *People* v. *Gym of America, Inc.*, 177 Colo. 97, 493 P.2d 660 (1972) (en banc), but we have not found any decisions holding that interpretations of Section 5 are binding on state administrative agencies and courts. On the contrary, several courts have held that although federal court decisions provide useful guidance, they are not controlling. *E.g.*, *State ex rel. Edmisten* v. *J.C. Penney Company, Inc.*, 292 N.C. 311, 233 S.E.2d 895 (1977).

Turning to the second question, we believe state courts would not be required to give weight to interpretations of language that might be added to the FTC Act. As for the states whose laws specifically refer to interpretations of Section 5(a)(1) of the FTC Act, the general rule of statutory construction is that "[a] statute of specific reference [one that refers specifically to a particular statute by its title or section number] incorporates the provisions referred to from the statute as of the time of adoption without subsequent amendments, unless the legislature has expressly or by strong implication shown its intention to incorporate subsequent amendments with the statute." 2A Sutherland, *Statutes and Statutory Construction*, § 51.07 (Sands ed. 1973); see *Hassett* v. *Welch*, 303 U.S. 303 (1938); see also *Department of Legal Affairs* v. *Rogers*, 329 So.2d 257, 267 (Fla. 1976) (Florida little FTC Act, which declares a legislative intent that "due consideration and great weight * * * be given to interpretations" of the Commission and the federal courts relating to Section 5(a)(1), "incorporates" only decisions of FTC and federal courts made prior to enactment of state statute). Fourteen statutes refer to Section 5 of the FTC Act, as amended,[11] but this lanugage apparently refers to amendments made to Section 5 prior to the enactment dates of the state statutes. See *State* v. *Julson*, 202 N.W.2d 145, 151 (N.D. 1972).

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§ 85-401(1); Neb. Rev. Stat. § 59-1617, § 87-304(a)(1); N.H. Rev. Stat. Ann. § 358-A:3; N.M. Stat. Ann. § 57-12-7; N.Y. Gen. Bus. Law § 349(d), § 350-c; Ohio Rev. Code Ann. § 1345.11(B), § 1345.12(A); Or. Rev. Stat. § 646.612(1); R.I. Gen. Laws § 6-13.1-5; S.C. Code Ann. § 39-5-40(a), (d); S.D. Codified Laws Ann. § 37-24-10; Tenn. Code Ann. § 47-18-111(a); Tex. Bus. & Com. Code Ann. § 17.49(b); Utah Code Ann. § 13-11-22(a); Va Code § 59.1-199; Wash. Rev. Code Ann. § 19.86.170; W. Va. Code § 46A-6-109(b); Wyo. Stat. § 40-11(a)(i).

[8] Ariz. Rev. Stat. Ann. § 44-1523; Ark. Stat. Ann. § 70-913(a); Del. Code Ann. tit. 6, § 2513(b); Iowa Code Ann. § 714.16; Mo. Ann. Stat. § 407.020(1); N.Y. Gen. Bus. Law § 349(d), § 350-c; S.C. Code Ann. § 39-5-40, (d).

[9] Ark. Stat. Ann. § 70-901; Cal. Bus. & Prof. Code § 17500; Colo. Rev. Stat. § 6-1-102; Del. Code tit. 6, § 25; Haw. Rev. Stat. § 481A; Ind. Code § 24-5-0.5; Iowa Code § 713-24; Kan. Stat. § 50-623; Ky. Rev. Stat. § 367.110; La. Rev. Stat. Ann. § 51:1401; Mich. Comp. Laws § 445.901; Minn. Stat. Ann. § 325.771; Miss. Code Ann. § 75-24-1; Mo. Ann. Stat. § 407.010; Neb. Rev. Stat. § 59-1601; Nev. Rev. Stat. § 598-360; N.J. Stat. Ann. § 56:8-1; N.Y. Gen. Bus. Law § 349; N.C. Gen. Stat. § 75-1; ND. Cent. Code § 51-15-01; Okla. Stat. Ann. tit. 15, § 751; Or. Rev. Stat. § 646.605; Pa. Stat. Ann. tit. 73, § 201-1; S.D. Comp. Laws Ann. § 37-24-1; Va. Code § 59.1-196; Wis. Stat. Ann. § 100.20; Wyo. Stat. § 40-102.

[10] Cal. Bus. & Prof. Code. § 17500; Kan. Stat. § 50-623; Mich. Comp. Laws § 445.901; Minn. Stat. Ann. § 325.771; Miss. Code Ann. § 75-24-1; Nev. Rev. Stat. § 598-360; N.J. Stat. Ann. § 56:8-1; N.C. Gen. Stat. § 75-1; N.D. Cent. Code § 51-15-01; Okla. Stat. Ann. tit. 15, § 751; Pa. Stat. Ann. tit. 73, § 201-1; Wis. Stat. Ann. § 100.20.

[11] 1981 Ala. Acts 81-355, § 6; Conn. Gen. Stat. Ann. § 42-110b(b); Fla. Stat. Ann. § 501.204; Ga. Code Ann. § 106-1201(c); Idaho Code § 48-604; La. Rev. Stat. Ann. § 1406(4); Me. Rev. Stat. Ann. tit. 5, § 207; Mass. Gen. Laws Ann. ch. 93A, § 2(b), (c); Mont. Code Ann. § 85-403; Ohio Rev. Code Ann. § 1345.02(C); R.I. Gen. Laws § 6-13.1-3; S.C. Code Ann. § 39-5-20(b); Vt. Stat. Ann. tit. 9, § 2453(b); W.Va. Code § 46A-103.

Question 12. The FTC has authority to issue its own subpoenas but, if the recipient of the subpoena resists, the FTC must seek enforcement of the subpoena in federal district court. Until the company decides to challenge the subpoena, the agency keeps all subpoena proceedings confidential. Most companies comply voluntarily with agency-issued subpoenas, often after negotiating their terms with agency staff, without resort to the courts.

What would a requirement that the agency go first to federal district court accomplish in terms of more rigorous court review?

What would such a requirement cost the government in terms of additional delay?

Wouldn't such a requirement have the effect of publicizing the existence of nonpublic investigations, even where the company would prefer to comply voluntarily and keep the investigation confidential?

How would this revision in the law increase the burdens on the federal court system?

Answer. What the requirement would accomplish in terms of more rigorous court review depends on the standard the courts would use in deciding whether to issue a subpoena. Courts will presently *enforce* a subpoena that the agency has issued "if the inquiry is whithin the authority of the agency, the demand is not too indefinite and the information sought is reasonably relevant." *United States* v. *Morton Salt Co.*, 338 U.S. 632, 652 (1950).

The requirement would cost the government additional delay by requiring it to go to court over each and every subpoena, however uncontroversial, reasonable, and necessary the demand for information.

Because "historically both civil and criminal trials have been presumptively open," *Richmond Newspapers, Inc.* v. *Virginia*, 448 U.S. 555, 580 n.17 (1980), S. 1984 would likely have the unintended effect of publicizing the existence of what would otherwise be nonpublic law enforcement investigations.

This revision in the law would increase the burdens on the federal court system by requiring the filing of lawsuits, and judicial determinations of those lawsuits, in each and every Commission law enforcement investigation that requires a subpoena. Allowing an administrative tribunal to issue subpoenas and dispose of motions to modify or quash them permits resolutions of disputes concerning the subpoenas before there is any need to resort to the judiciary. S. 1984, however, would place the entire burden on the courts. Moreover, depending on the standards that would govern judicial determinations whether to issue subpoenas, the courts would be required to decide, among other things, what documents should be sought, what constitutes a reasonable request, and how great is the likelihood of law violations.

Question 13. Does any other agency or department of the federal government currently pay the costs of complying with its own subpoenas?

As a practical matter, wouldn't such a requirement have the effect of focusing the agency's attention almost exclusively on small business since it would have limited resources to investigate major matters involving large national corporations?

Answer. Under present legal requirements, agencies generally must reimburse a complying party for costs that "exceed * * * that which a party ought reasonably be made to shoulder." *SEC* v. *Arthur Young & Co.*, 584 F.2d 1018, 1033 (D.C. Cir. 1978), cert. denied, 439 U.S. 1071 (1979). We are unaware of any agencies of departments that pay all the costs (including a party's attorneys' fees) of complying with every subpoena.

I cannot now say that, as a practical matter, S. 1984 would "have the effect of focusing the agency's attention almost exclusively on small business since it would have limited resources to investigate major matters involving large national corporations." However, depending on the size of the claims for reimbursement of compliance costs and attorneys' fees, we could not do an adequate job of law enforcement and investigation and our ability to conduct large-scale law enforcement investigations would certainly be restricted.

Question 14. In your letter to me dated February 16, 1982, you said that ". . . the Commission voted last October 21 to reduce the number of regional offices from ten to six, with Commissioner Pertschuk dissenting." As the enclosed colloquy between myself and Senator Weicker on November 12, 1981 indicates, in passing the Kasten amendment to reduce funding for the FTC to $68.1 million in the 1982 Appropriations Bill, the Senate believed that this FTC decision to reduce the number of regional offices was based upon anticipation of an 1982 appropriations reduction to $61,123,000, and that in the case of an appropriation of at least $68.1 million, ". . . the Commission would look anew at the question of whether the number of regional offices should be reduced." In your prepared statement for the March 16, 1982 FTC reauthorization hearing of this Committee, you stated that the Commission ". . .

does not object to the President's recommended funding levels for the pertinent years, i.e., no less $60.8 million (fiscal year 1983), $55.1 million (fiscal year 1984), and $54.6 million (fiscal year 1985)." I understand that the 1983 further cut would be accomplished principally by reducing the number of regional offices from ten to six. If, however, Congress in its wisdom, decided to fund the FTC at no less than the 1982 level in 1983 (and beyond), how would the decision to reduce the number of regional offices be affected?

Answer. From my standpoint, the Commission's decision to restructure the regions was a management decision and not simply a budget decision. While it is true that this decision was made by the Commission in the context of budget discussions, it was not made contingent upon budget factors.

The Commission's decision to restructure the regions into six offices reflects the Commission's interest in maximizing the effectiveness of resource and workyears available to the Commission.

Based on revisions in OMB Circular A-10, I cannot respond to questions concerning how funding in excess of the President's recommendation might be applied.

Question 15. As originally conceived, the FTC is an administrative agency with substantial expertise in the fields of economics, antitrust and consumer protection. The Commission was given authority to try its own cases in the first instance so that it could bring this expertise to bear on the development of basic case law under Section 5. All FTC decisions are reviewable by federal appellate courts.

What are the justifications for changing the agency's fundamental role and requiring it to try its cases in the first instance before a federal district court?

Why doesn't federal appellate court review accomplish the goal of judicial supervision of the agency's interpreation of its statutory mandate?

What kind of burden would such a change place on the federal district court system?

Answer. Advocates of a repeal of the Commission's adjudicatory function have argued that it is inherently unfair for the agency that issued a complaint to decide the case. They also argue that judicial review is an insignificant safeguard because review, is limited and the Commission's findings are given great weight.

Nevertheless, there is nothing unique about the combination of prosecutorial and adjudicatory functions. According to Professor Davis, a leading commentator on administrative law and procedure, "the very identifying badge of the modern administrative agency is the combination in the same hands of the judicial power to adjudicate cases and the legislative power of rulemaking, along with the executive powers to enforce, to investigate, to initiate and to prosecute." 1 K. Davis, *Administrative Law Treatise* 71 (2d ed. 1978). The courts have consistently held that this combination of functions is not unfair. E.g., *Withrow* v. *Larkin*, 421 U.S. 35 (1975).

Orders to cease and desist, issued by the Commission, are subject to judicial review under the strict substantial evidence standard, based on the court's review of the entire record. The courts of appeals and the Supreme Court have the ultimate responsibility for determining that the law has been violated—that the Commission's order is supported by the evidence and that its interpretations of Section 5 are correct. See, e.g., *FTC* v. *R.F. Keppel & Bros.*, 291 U.S. 304, 314 (1934).

In response to your question, I believe that requiring the Commission to bring its cases in federal district court would impose a significant burden on the federal court system. S. 1984 would fragment the decisional process among more than 500 district judges and impose upon them the responsibility for resolving what are often complex issues of economics and public policy. They would face an almost impossible burden if they were expected to achieve what the 1914 Congress that created the Federal Trade Commission intended: a "centralized and orderly development of precedent applying the regulatory statute to a diversity of fact situations." *Holloway* v. *Bristol-Myers Corp.*, 485 F.2d 986, 998 (D.C. Cir. 1973).

In sum, I think my mind is not closed on this matter, and while I concede that those who argue for a separation of prosecutorial and adjudicating functions have a point, at this time I feel that the current arrangement is the preferred configuration.

Question 16. I have no doubt that a strong majority of Congress believes that the FTC should maintain a viable regional structure. As the 1982 Senate Appropriations Committee Report indicated, the regional offices" . . . have a major role in working with the small business communities in their areas, in identifying local anticompetitive problems, in enforcing antitrust laws, and in explaining to businesses their rights and responsibilities under numerous Federal statutes." Jared O. Blum, on behalf of the Small Business Legislative Council, said in his statement before this Committee at the FTC reauthorization hearing on March 18, 1982:

"Enforcement of the rules of competition in the market areas where they are taking place is of vital concern to small business. Small business need an antitrust presence—a cop on the beat . . . If cut backs in regional offices are inevitable, . . . we urge this Committee and the Federal Trade Commission to see to it that a regional office structure that is evenly distributed geographically and which is designed to maintain strong Commission presence is preserved."

In your letter to me of February 16, 1982, you said that in making decisions about closing regional offices, you would "be guided by a careful evaluation of the past effectiveness of each regional office, particularly as it reflects on the potential efficiency and future plan of the office." Will relatively even geographic distribution be an important factor in these decisions? There are currently three regional offices on the Pacific Coast.

Are you seriously considering making two of your anticipated for nationwide closure from among these three offices?

If not, are you seriously considering closing the Seattle regional office and leaving two Pacific Coast offices, both located in the State of California?

Answer. The restructuring of the FTC's regional office structure was based on a number of factors, and each Commissioner undoubtedly applied his or her own criteria. Clearly, however, geographic distribution was a factor. My own view is that, based on the geographic considerations above, it is sensible to consolidate the three west coast regional offices into one office—the one in San Francisco.

QUESTIONS OF SENATOR KASTEN AND THE ANSWERS THERETO

Question 1. Please submit a list of cases won by the Commission on an unfairness theory.

Anwer. The Commission has won a number of litigated cases on an unfairness theory. The most important of these can be grouped under seven general headings.

1. All-State Industries, 75 F.T.C. 465 (1969) (alternative ground), aff'd 423 F. 2d. 423 (4th Cir.), cert. denied, 400 U.S. 828 (1970). This was the first important case to use the unfairness theory. It held that it was unfair for a contractor to unexpectedly sell a consumer note to a holder in due course, thereby cutting off any claim that the consumer might have for reduced payment on the basis of faulty workmanship or similar factors.

2. FTC v. *Sperry & Hutchinson Co.,* 405 U.S. 233 (1972). In this case the Supreme Court accepted, as a matter of principle, that an action could be brought on a theory of consumer unfairness. The case involved efforts by S&H to suppress the operation of exchanges which allowed consumers to trade one kind of premium stamp for another.

3. Gambling cases.—Beginning in the 1930's the Commission successfully challenged a number of firms for including a gambling element in their sales contracts as an inducement for people to buy. The practices were determined to be unfair as a violation of the established public policy of that period—although, of course, they would presumably not be so considered under the different standards of today. The cases included *FTC* v. *R. F. Keppel & Bro.,* 291 U.S. 304 (1934); *Wolf* v. *FTC,* 135 F. 2d 564 (7th Cir. 1943); *Feitler* v. *FTC.* 201 F. 2d 790 (9th Cir.), cert. denied, 346 U.S. 814 (1953); *Gellman* v. *FTC* 290 F. 2d 666 (8th Cir. 1961).

4. Dangerous advertisements.—In another group of cases the Commission challenged advertisements that, although not deceptive, created a risk of injury for small children watching them. The cases included *Philip Morris,* 82 F.T.C. 16 (1973) (consent decree) (free-sample razor blades mailed in such a way that children might find and open them); *AMF, Inc.,* 95 F.T.C. 310 (1980) (television ad showed children riding bicycles into street without looking for cars, creating risk that viewers would emulate what they saw); *Uncle Ben's* 89 F.T.C. 131 (1977) (ad showing children cooking by themselves without close adult supervision, again tempting emulation); General Foods, 86 F.T.C. 831 (1975) (ad showing natural food advocate eating unidentified plants found in the woods).

5. Coercive practices.—Another group of cases banned, as unfair, overbearing sales practices which were substantially coercive to the customers involved. Examples include *Holland Furnace Co.* v. *FTC,* 55 F.T.C. 55 (1958), aff'd, 295 F.2d 302 (7th Cir. 1961) (dismantling home furnaces for a free 'inspection" and then refusing to reassemble them until customers bought additional parts or services); (*Arthur Murray* v. *FTC,* 458 F.2d 622 (5th Cir. 1972) (elderly female customers pressured into signing for long series of dance lessons during sales sessions sometimes lasting several hours and using relays of salesmen); *Medi-Hair International,* 80 F.T.C. 627 (1972) (consent decree) (intense, emotional pressure used to entice customers to sign contract for treatment of baldness).

6. Improper remedies.—In this group cases the Commission kept sellers from using excessively harsh or abusive remedies after a dispute arose with the customer. Among these cases are *Spiegel* v. *FTC*, 540 2d 287 (7th Cir. 1976) (banning seller from bringing collection suits in courts whose distant location violates the principles of due process); *Capital Builders* 92 F.T.C. 274 (1981) (consent decree) (banning self-help) repossessions through intimidation, threats, or deception); *Ford Motor Co.*, 94 F.T.C. 564 (1979) (ordering automobile dealers to refund any surplus realized after customers' cars repossessed and sold), rev'd on other grounds, Nos. 79-7649 & 79-7654 (9th Cir. 1981).

7. Rules requiring the disclosure of essential information.—A final area of Commission activity involves rules requiring sellers to provide certain pieces of critical information that consumers need in order to make reasonably knowledgeable purchase decisions. These matters are not technically "cases" and they do not technically come within the terms of this question. Since they represent the Commission's most important recent initiatives in the field of consumer unfairness, however, it seems desirable to make some mention of them as well. Recent informational rules include Care Labeling of Textile Wearing Apparel, 16 C.F.R. § 423 (1981) (requiring clothes to include labels giving washing instructions); Advertising of Ophthalmic Goods and Services, 43 Fed. Reg. 23,992 (1978) (prohibiting restrictions on price advertising) (rule later withdrawn for consideration of mootness); Labeling and Advertising of Home Insulation, 16 C.F.R. § 460 (1981) (requiring disclosure of the R-Value of insulation).

Question 2. Please submit a list of cases involving advertising brought by the Commission on an unfairness theory.

Answer. Since FTC complaints and orders uniformly plead that an act or practice is "unfair and deceptive," it is not easy to find advertising cases based solely on an unfairness theory. In *Pfizer, Inc.*, the Commission held that failure to possess a rea sonable basis for an affirmative product claim in advertising was unfair. 81 F.T.C. 23, 64 (1972). Subsequent reasonable basis cases have been premised primarily on deception.

The following consent orders, although based upon deception and unfairness, relied heavily on unfairness for their rationale. All four concern advertising which showed children and/or adults engaged in unsafe behavior or portrayed situations which might encourage unsafe actions by children. These advertisements could also be labeled as deceptive by arguing that they implicitly claim that the behavior portrayed is safe.

Uncle Ben's Inc., 89 F.T.C. 89 F.T.C. 131 (1977) (ad portrayed children cooking at a stove without adult supervision).

Mego Industries, Inc., 92 F.T.C. 186 (1978) (ad portrayed child using electrical appliance near sink of water without adult supervision).

General Foods Corp., 86 F.T.C. 831 (1975) (ad portrayed Euell Gibbons eating wild plants in ad for Grape-Nuts; ad might influence children to experiment with wild plants).

AMF, Inc., 95 F.T.C. 310 (1980) (ad showed children riding bicycles in unsafe manner).

Question 3. Please submit a list of cases brought by the Commission in the last 15 years that could not have been initiated under your proposed definition of deception.

Answer. I have attached a list of cases that I relied upon in my testimony (See Attachment #1.) Most these cases were brought during the 1970's. The list includes some earlier cases, because they indicate the wide discretion available to the Commission in its consideration of the deceptiveness of a particular claim.

It would be extremely difficult to determine all of the cases that the proposed standard would preclude. The standard would require the Commission to address factual questions that it has not always considered in the past. Even if a detailed review of the record in a past case indicated that the Commission could not have acted under the new standard, the Commission might have prevailed had it developed the appropriate evidence. Thus, I have provided a list of examples of past problems, rather than a complete list of all past cases.

Question 4. Please submit an analysis of the difference between deception as it has been applied by the Commission and deception as you would propose to define it.

Answer. I have attached a memorandum prepared by Timothy J. Muris, Director of the Bureau of Consumer Protection. (Attachment #1.) This memorandum contains a detailed analysis of the current standard of deception and the need for changes. There are two principal differences between the current and proposed definitions of deception. Under the latter, first, the Commission could pursue only those claims that reasonable consumers would draw from the ad under the circumstances. Second, the claim would have to be one that would be likely to cause consumer injury.

Under the current standard of deception, the Commission can proceed against claims that only unreasonable consumers would draw from an ad. Commission action against such claims harms reasonable consumers, who do not perceive those claims, by prohibiting or otherwise limiting the advertisement. Such advertising provides truthful and useful information to the majority who interpret it reasonably. The proposed definition would limit Commission action in such cases.

Currently, the Commission need not prove that a deceptive practice is likely to harm consumers. To the extent that the Commission must find that consumers are injured, and few cases require such a finding, the Commission's reliance on its own expertise has undermined the requirement. The Commission wastes the taxpayer's resources when it seeks to prevent advertising which is to protect consumers. Under the proposed definition, the likelihood of injury may be a logical inference, subject to rebuttal by the respondent's evidence. There are several ways that the Commission could prove the likelihood of injury. For instance, is the product likely to be worth more to consumers if the representations are accurate? If the answer is in the affirmative, the likelihood of injury may exist.

A statutory standard for deception would eliminate certain cases that I believe should not be brought. It would not, however, substantially complicate those cases when the Commission should clearly act. Often, likelihood of consumer injury can be inferred without elaborate evidence, and the meaning reasonable consumers will take from an ad is apparent on the face of the ad. In cases when it is not clear whether the Commission should act, the proposed definition would require the Commission to develop external evidence, rather than relying solely on its expertise. In a government of laws, not men, it is entirely appropriate that one should consider the evidence before one acts.

QUESTIONS OF SENATOR FORD AND THE ANSWERS THERETO

Question 1. What advertising cases have been brought under Section 5 using strictly "unfairness" as the standard for a complaint? Would the FTC be unable to bring certain cases that it has brought in the past if this authority were eliminated? For the record, would you summarize any such advertising cases brought since 1972?

Answer. Since FTC complaints and orders uniformly plead that an act or practice is "unfair and deceptive," it is not easy to find cases based solely on an unfairness theory. The following consent orders, although based upon deception and unfairnes, relied heavily on unfairness for their rationale. All four concern advertising which shoed children and/or adults engaged in unsafe behavior or portrayed situations which might encourage unsafe actions by children. These advertisements could also be labeled as deceptive by arguing that they implicitly claim that the behavior portrayed is safe.

Uncle Ben's Inc., 89 F.T.C. 131 (1977) (ad portrayed children cooking at a stove without adult supervision).

Mego Industries, Inc., 92 F.T.C. 186 (1978) (ad portrayed child using electrical appliance near sink of water without adult supervision).

General Foods Corp., 86 F.T.C. 831 (1975) (ad portrayed Euell Gibbons eating wild plants in ad for Grape-Nuts' ad might influence children to experiment with wild plants).

AMF, Inc., 95 F.T.C. 310 (1980) (ad showed children riding bicycles in unsafe manner).

Question 2. Could the "razor blade case," cited by some as needed for an "unfairness" standard in commercial advertising cases under Section 5, have been brought as an unfair act or practice under current law? (But not as a commercial advertising case; based on the "conduct" of distributing the razor blades.)

Answer. I believe the Commission could have proceeded against the company for its unsafe distribution of razor blades in newspapers as an unfair practice. In fact, there is no mention in the complaint or the order of advertising. The complaint alleges that:

"the distribution of sample razor blades directly to members of the general public by means of home-delivered newspapers . . . constitutes a hazard to health and safety of persons engaged in the distribution of newspapers and persons receiving such newspapers in their houses, particularly young children, and also to family pets." 82 F.T.C. 16, 17.

The order does not cover advertising, but distribution. Id. at 19. Thus, the razor blade case is not really an advertising case, but a distribution or conduct case.

Question 3. Could the "razor blade case" have been brought as unfair act or practice under the new proposed definition of unfairness?

Answer. I believe the razor blade case could be brought under the proposed definition of unfairness. First, the likelihood of substantial injury exists, particularly to young children who might open the newspaper, unsupervised by an adult, discover the razor blade and start playing with it. As is common knowledge, even adults who know how to use razor blades can injure themselves accidentally. Children, who do not have the same appreciation for the sharpness of the blade as do adults, are much less likely to use the appropriate care with the blade, and thus much more likely to inflict substantial injury on themselves.

Second, the injury is not outweighed by an off-setting benefit. The order allows the company to distribute razor blades in newspapers as long as theire is a clear disclosure that a razor blade is present and the blade is enclosed in special packaging, constructed to be significantly difficult for children under six to open within a reasonable time.

Third, the injury from the razor blade, as it was originally distributed, could not have been reasonably avoided by the children, or the newspaper deliverers, because they did not know that the razor blades were present. In the case of children, as mentioned above, they probably do not have the appreciation that adults have for the substantial physical risk that an unsafe use of razor blades poses.

Question 4. You have personally recommended defining deceptive acts or practices. What cases have been brought by the FTC in the last ten years that could not be brought under your proposed definition? Could you provide a complete list of these cases for the record? (Case citation—a short factual summary and ultimate disposition.)

Answer. I have attached a list of cases that I relied upon in my testimony. (See attached memorandum.) Most of these cases were brought during the 1970's. The list includes some earlier cases, because they indicate the wide discrection available to the Commission in its consideration of the deceptiveness of a particular claim.

It would be extremely difficult to determine all of the cases that the proposed standard would preclude. The standard would require the Commission to address factual questions that it has not always considered in the past. Even if a detailed review of the record in a past case indicated that the Commission could not have acted under the new standard, the Commission might have prevailed had it developed the right kinds of evidence. Thus, I have provided a list of examples of past problems, rather than a complete list of all past cases.

Question 5. What rulemakings that were initiated by the FTC could not be initiated under your deception definition?

Answer. The proposed definition would require the Commission to find certain facts before it could determine that an act or practice was deceptive, whether in an individual case or in a rulemaking. If the Commission can establish that a reasonable interpretation of a communication is false, and that the false claim is likely to lead to consumer injury, it could issue a rule based on the new deception standard, just as it does under current law. As to rulemakings that are currently pending, I should not comment on whether these factual conditions are met, because I will soon be called upon to make a decision on these facts. As to prior proposals, I believe it would have been very difficult for the Commission to propose the Children's Advertising rulemaking under the new definition of deception. The staff argued that all advertising to young children was inherently deceptive, because young children cannot understand the selling purpose of advertising. Under the proposed standard, the Commission would have to show that an ordinary child would interpret these advertisements in a way that was incorrect, and that this incorrect interpretation would lead to injury. I do not believe that this burden could be met.

Question 6. What cases could not be brought, if "unfair methods of competition" authority was limited to Sherman and Clayton violations as the Chamber of Commerce has suggested? Could you list for the record all the cases brought since 1965 that fit into this category? Please provide the case citation, summary of the facts, and the ultimate outcome of the case.

Answer. The Federal Trade Commission uses its "unfair methods of competition" authority not only to reach activities that violate the Sherman Act or Clayton Act, but also to challenge incipient violations of those statutes and to prevent conduct that violates their spirit. The Commission can deal satisfactorily with most anticompetitive conduct by using Sherman and Clayton Act standards. On occasion, though, the Commission's "unfair methods of competition" authority is uniquely well-suited for prevention of particular anticompetitive practices. While infrequently used, this authority helps the Commission preserve a vigorous competitive marketplace through prospective cease and desist orders without the financial risk and penalties to the affected companies associated with retroactive Sherman and Clayton Act enforcement. Limiting the Commission's "unfair methods of competition" authority to violations of the Sherman and Clayton Acts would eliminate a law enforcement tool that is valuable as a supplement to the other antitrust laws.

The Commission and any court reviewing an FTC order must decide whether a respondent corporation has committed an "unfair method of competition." They usually do so without making any determination whether the same conduct could have been reached under the Sherman Act or Clayton Act. In some cases, it is not clear, therefore, how much it would impinge on effective law enforcement if the Commission's "unfair methods of competition" authority were limited to prosecution of Sherman and Clayton Act violations. Such a legislative change would at a minimum create substantial confusion and uncertainty in the business community about the continued vitality of longstanding rulings by the Commission on a wide range of practices found to threaten serious injury to competition and the public. These cases fit into three basic categories.

First, Section 5 has been used to fill "gaps" in the Clayton Act. The Commission used its "unfair methods of competition" authority to supplement Section 7 of the Clayton Act in one recent case, for example, by finding the seller of stock, instead of just the buyers, to be legally responsible for its involvement in an anticompetitive acquisition, thereby permitting achievement of a more equitable and effective remedy. In a number of Commission cases, respondents have been found liable for inducing and receiving discriminatory promotional allowances. While the Robinson-Patman Act provisions of the Clayton Act only prohibit the granting of discriminatory promotional allowances, their inducement and receipt by powerful purchases who benefit from them violate the spirit of the Act and are reachable under Section 5. A contrary rule of law would be anomalous.

Second, Section 5's proscription of "unfair methods of competition" can supplement the Sherman Act in several ways. It has been used to challenge anticompetitive, interdependent behavior engaged in by more than one firm that may not be the product of a provable agreement. For example, the Commission has ruled that interdependent use of base-point pricing, where it results in a substantial lessening of competition, is an unfair method of competition. In another case, now on appeal to the Commission, the Administrative Law Judge found that the respondent corporations violated Section 5 by interdependently engaging in pricing-related practices that lessened competition and resulted in supracompetitive prices. Section 5 has also been used to challenge dominant firm conduct causing serious injury to competition, but falling short of attempted monopolization in violation of the Sherman Act. In one case an oil company agreed to a consent order prohibiting it from using its power over its independent service station dealers to force them to carry only automobile accessories manufactured by that company. The Commission has also used Section 5 to challenge arbitrary abuses of monopoly power that restrain competition in adjacent markets, a use of Section 5 on which the courts seem to be divided, pending resolution by the Supreme Court. In a recent proceeding, the Commission held that the publisher of the only comprehensive schedule for domestic airlines had acted unlawfully in discriminating arbitrarily between different classes of air carriers, causing substantial injury to consumers and to competition among the air carriers. The FTC's order was overturned by the Second Circuit Court of Appeals, whereas it might have been upheld under applicable precedent in the Fifth Circuit.

Third, Section 5 is used to prevent unfair competition akin to business torts that cause serious injury to competition, such as commercial bribery, kickbacks and "payola" that might not be reachable under the Sherman Act. In one recent order, for example, a major medical laboratory chain agreed not to give kickbacks to physicians who referred patients to its facilities, where the challenged payments allegedly lessened competition and injured competing laboratories that did not make illegal payments.

Listed below are cases initiated by the FTC since 1965 that probably could not have been brought, as they were pleaded, under the Clayton or Sherman Acts. It is possible, however, that some cases included or could have been pleaded as Clayton or Sherman Act violations.

CASES FILLING "GAPS" IN THE CLAYTON ACT

1. Section 2: The Robinson-Patman Act

Times-Morror, Co., Inc., Docket 9103, complaint filed Aug. 16, 1977 (complaint alleging price discrimination in sale of advertising space withdrawn to all Commission to evaluate proposed consent order).

Herbert Gibson, Sr., 94 F.T.C. 553 (1980) (count of complaint charging that respondents induced discriminatory promotional allowances from suppliers dismissed by Commission).

Alterman Foods, Inc., 82 F.T.C. 298 (1973); affirmed 497 F.2d 993 (5th Cir. 1974) *Individualized Catalogs, Inc.*, 76 F.T.C. 80 (1969); *Best & Co., Inc.*, 72 F.T.C. 422 (1967) (Commission entered orders to cease and desist after finding that respondents in each case had induced or received discriminatory promotional allowances or services from suppliers).

Zayre Corp., 93 F.T.C. 94 (1979); *Thrifty Drug Stores Co., Inc.*, 87 F.T.C. 800 (1976); *The Kroger Co.*, 83 F.T.C. 458 (1973); *Foremost-McKesson, Inc.*, 83 F.T.C. 228 (1973); *Western Storecasting, Ltd.*, 82 F.T.C. 1138 (1973); *Buy-Rite Foods, Inc.*, 80 F.T.C. 970 (1972); *Times Square Stores Corp.*, 70 F.T.C. 519 (1966); *Peck and Peck*, 69 F.T.C. 786 (1966); *Robert Carp.*, 68 F.T.C. 1027 (1965); *Pacific Gamble Robinson Co.*, 71 F.T.C. 284 (1967) (consent orders settling complaints that respondents had induced or received discriminatory promotional allowances or services from suppliers).

2. Section 7: acquisitions

Brunswick Corp., 94 F.T.C. 1174 (1979), *order entered*, 96 F.T.C. 151 (1980), *aff'd Yamaha Motor Co., Ltd. v. FTC*, 657 F.2d 971 (8th Cir. 1981); *Dean Foods Co.*, 70 F.T.C. 1146 (1966) (sellers of stock and assets held to violate Section 5 when effect of sale is to restrain competition substantially).

Lone Star Cement Co., 71 F.T.C. 35 (1967); *Ideal Cement Co.*, 69 F.T.C. 762 (1966) (consent orders settling complaints alleging restraint of competition through acquisitions of companies not doing business in interstate commerce). Such acquisitions were recently made subject to the Clayton Act. Antitrust Improvements Act of 1980, P.L. 96-349, § 61, Stat. 1167 (1980).

Ash Grove Cement Co., 85 F.T.C. 1123 (1975), affirmed, 577 F.2d 1368 (9th Cir. 1978) (Commission dismissed, for failure of proof, count of complaint alleging that acquisition of assets from individuals restrained competition). Such acquisitions were recently made subject to the Clayton Act. Antitrust Improvements Act of 1980, P.L. 96-349, § 61, 94 Stat. 1167 (1980).

SKF Industries, Inc., 94 F.T.C. 6 (1979) (Commission dismissed, for failure of proof, count of complaint alleging that respondent's acquisition of foreign manufacturers not doing business in the United States was part of a plan to reduce competition in the United States by eliminating firms that were potential competitors in the market).

Murata Mfg. Co., Ltd., 96 F.T.C. 1116 (1980); *Bendix Corp.*, 96 F.T.C. 352 (1980); *Liquid Air Corp. of North America*, 94 F.T.C. 390 (1979); *Lone Star Industries, Inc.*, 94 F.T.C. 341 (1979); *Lancaster Colony Corp.*, 93 F.T.C. 318 (1979) (consent orders settling complaints alleging that respondents had agreed to enter into mergers that, if consummated, would have violated the Clayton Act).

Grand Union Co., F.T.C. Docket No. 9121, complaint filed Nov. 21, 1978, appeal pending (Administrative Law Judge dismissed count of complaint charging that respondent acted illegally by entering new region of country by most anticompetitive means available to it).

3. Section 8: interlocks

Perpetual Federal Savings & Loan Association, 90 F.T.C. 608 (1977) *order withdrawn*, 94 F.T.C. 401 (1979) (Commission found interlocking directorates between bank and savings and loan association illegal; complaint dismissed after passage of Depository Institution Management Interlocks Act of 1978), 92 Stat. 3672, 12 U.S.C. § 3201, that bars such interlocks in the future, but exempts them from challenge for 10 years, and legislation removing savings and loan associations from FTC jurisdiction).

CASES SUPPLEMENTING THE SHERMAN ACT

1. Alleged anticompetitive interdependent practices

Ethyl Corp., FTC Docket No. 9128 (Initial Decision Aug. 5, 1981, appeal pending) (complaint alleges that the four domestic producers of lead-based antiknock compound restrained price competition unlawfully by interdependently using certain marketing practices that facilitated pricing coordination; violation found by administrative law judge; appeal pending before Commission).

Kellogg Co., FTC Docket No. 8883 (Initial Decision Sept. 1, 1981, complaint dismissed January 15, 1982) (cereal manufacturers' use of exclusionary marketing practices allegedly resulted in high entry barriers and supracompetitive pricing, administrative law judge found charges unproven, complaint dismissed).

Boise Cascade, 91 F.T.C 1 (1978), *enforcement denied*, 637 F. 2d 573 (9th Cir. 1980) (Commission found that interdependent use of base-pint pricing by plywood manufacturers had substantially lessened competition and was unfair method of competition; reversed on appeal apparently for indadquate evidentiary basis for FTC ruling).

2, Alleged anticompetitive conduct by dominant firms

Phillips Petroleum Co., 84 F.T.C. 1666 (1974) (consent order settling complaint alleging that respondent used its market power to force its independent service station dealers to distribute only tires, batteries, and accessories manufactured by respondent).

Georgia Pacific Corp., 83 F.T.C. 1428 (1973) (consent order settling complaint alleging that respondent corporation had systematically used its purchasing power to obtain reciprocal sales of its products to certain of its suppliers, which gave respondent an unfair competitive advantage and caused injury to the public).

Federated Department Stores, Inc., 93 F.T.C. 449 (1979) (consent order settling complaint alleging that operator of department stores had entered into agreements with shopping centers allowing it to exclude potential tenants from the shopping centers, thereby lessening price competition among retail outlets).

Tysons Corner Regional Shopping Center, 85 F.T.C. 970 (1975), modified 86 F.T.C. 921 (1975) (Commission entered cease and desist order after finding that shopping center developer's grant of veto power over other prospective tenants to major department store was similar in effect to a boycott and posed serious dangers to price competition).

3. Alleged abuses of monopoly power

General Motors Corp. (Crash Parts), FTC Docket No. 9077, Initial Decision, Sept. 24, 1979, appeal pending (complaint alleged, inter alia, that respondent abused its monoply power in the market for replacement crash parts for cars manufactured by it by refusing to supply parts to independent repair shops competing with its franchised dealers, thereby impairing competition for repair services and injuring consumers; administrative law judge found no violation on this point; case has been appealed by both sides to the Commission).

Reuben E. Donnelly Corp., 95 F.T.C. 1, *rev'd sub nom. Official Airlines Guides* v. *FTC*, 630 F. 2d 920 (2d Cir. 1980), *cert. denied, 450* U.S. *917*, (1981) (Commission held that arbitrary discrimination between classes of air carriers by the only publisher of comprehensive airline schedule, that caused injury to competition among air carriers, was an unfair method of competition; court of appeals reversed, finding no duty of nondiscrimination by monopolist).

BUSINESS TORTS AND UNFAIR COMPETITION

McDonnell Douglas Corp., 92 F.T.C. 976 (1976). *Boeing Co.*, 92 F.T.C. 972 (1978); *Lockheed Corp.*, 92 F.T.C. 968 (1978) (consent orders settling complaint alleging that aircraft manufacturers had made payments to foreign officials to influence their purchase decisions, effective excluding other domestic aircraft manufactures from those markets).

Damon Corp. 91 F.T.C. 301 (1978) (consent order settling complaint alleging that a major medical laboratory chain had made improper payments to physicians for referral of tests chargeable to patients to Damon rather than to its competitors, thereby giving Damon an unfair competitive advantage, causing overall consumer costs to increase, and stabilizing laboratory test prices at higher levels).

Question 7. Should rulemaking authority under Section 6(g) be utilized to initiate "fact intensive" antitrust rules?

Answer. Section 6(g) of the Federal Trade Commission Act is the statutory basis for the Commission's antitrust rulemaking authority. *In National Petroleum Refiners Association* v. *FTC*, 482 F. 2d 672 (D.C. Cir. 1973), cert. denied, 415 U.S. 957 (1974), the federal court of appeals held that Section 6(g) authorizes the Commission to promulgate substantive, as well as procedural rules.[1] Open panel medical prepayment plans, the Commission published an advance notice of a proposed rulemaking in this area, and requested public comments on this approach.[2] However, after reviewing these comments, the further analysis, the Commission determined last year that an industrywide rule was not the appropriate way to address these concerns. Rather, the Commission decided to proceed on a case-by-case basis because . . . medical control of prepayment plans is not always anticompetitive . . . and because it may not be feasible to devise a rule that clearly distinguishes between procompetitive and anticompetitive agreements. Analysis of the competitive impact of such agreements in a particular case may often require consideration of a variety of factors, . . . [and] [s]ince an across-the-board rule cannot readily take all these factors into account, a rule might in some situations prevent the development of procompetitive prepayment plans. 46 Fed. Reg. 27,768 (1981).

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[1] See also Katherin Gibbs School (Inc.) v. FTC, 612 F. 2d 658, 661 (2d Cir. 1979).

Thus the Commission is sensitive to the need to limit antitrust rulemaking only to circumstances where it will not be overly broad and will include only those factual situations which are demonstrably anticompetitive.

The Commission's Section 6(g) rulemaking authority is also subject to numerous checks and limitations to assure that this autority is not abused. Any rules must be promulgated in accordance with the Administrative procedure Act's procedural requirements, including federal court review, and further, are currently subject to congressional veto provisions.

Section 6(g) rules basically serve only to clarify the law applicable to particular conduct. Enforcement of antitrust rules by the Commision requires issuance of a Commision complaint as in all FTC adjudicative proceedings, and trial before an adminitrative law judge to determine whether the standards set out in the rule have been violated. Any final decision adverse to a respondent corporation is appealable to the federal courts. The Commission is limited to obtaining cease and desist orders against conduct violative of Section 6(g) antitrust rules. Unlike enforcement of Magnuson-Moss Act consumer protection rules, no monetary penalties are available for violation of Section 6(g) rules; rather, the Commission is limited to obtaining prospective relief only.

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[2] 45 Fed. Reg. 17019 (1980).

[ATTACHMENT 1]

FEDERAL TRADE COMMISSION,
March 25, 1982.

Memorandum for the Chairman.
From: Timothy J. Muris, Director.
Subject: Defining Deception.

I. INTRODUCTION

As you requested, this memorandum discusses my views regarding the deception doctrine. In brief, I believe that an act or practice is deceptive if it would mislead consumers, acting reasonably in the circumstances, to their detriment. For cases involving vulnerable groups, the Commission should be able to proceed without necessarily meeting this two-part standard of reasonable interpretation and consumer injury. With this definition, the Commission's law of deception would better protect consumers, while providing better guidance to staff and to the business community.

Those who oppose any changes regarding the deception doctrine argue that because nothing is broken, there is nothing to fix. I disagree. Review of the Commission's most recent advertising decision, Kroger,[1] belies that premise, suggesting instead that the Commission's law of deception is in need of repair.

Kroger's advertising described the results of its "Price Patrol," in which homemakers surveyed prices of 100 to 150 items in local supermarkets. The Commission conceded that "the evidence does not dispute Kroger's basic argument that its prices were frequently below or equal to those of its competitors."[2] Nevertheless, based on its own expertise, without evidence of the advertising's meaning, the Commission held that the ads were deceptive because they implicitly represented that the surveys were "methologically sound" and "statistically projectible."

Commissioner Bailey dissented. She noted that Kroger made a point of emphasizing the informality of the surveys. She continued: "[t]he notion that these surveys were 'methologically sound' and therefore 'prove' an overall 'projection' of lower prices is simply, in my view, an artificial construct imposed by the majority [of the Commissioners] on the ads in question."[3]

I agree with what Commissioner Bailey said in Kroger. Kroger, as well as the other FTC decisions discussed in Appendix A, reveal the four major problems with many FTC deception cases. First, the Commission relied on its own expertise, without evidence of how consumers would understand the ads. The interpretation of advertising should not be left solely to the subjective judgments of the Commissioners, who have almost always been lawyers with no special background in advertising or other aspects of the communications business. Second, the Commission's interpretation of the ad was not based upon what consumers acting reasonably in the circumstances would understand the ad to mean. As Commissioner Bailey noted, the advertising's informality seemed to make the Commission's interpretation an unreasonable one.

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[1] Kroger Co., D. 9102 (Sept. 25, 1982).

[2] Id. at 18.

[3] Id., dissent at 3.

Third, even accepting the Commission's interpretation of the ads, there was no evidence that consumers were likely to have been injured. Because the Commission found that Kroger's prices were frequently below or equal to those of its competitors, how did the alleged "deception" harm anyone? Fourth, the decision is likely to harm consumers. Although consumers find comparative price advertising useful, the Commission's reading of the ads increased Kroger's difficulty in communicating comparative information to consumers. As Commissioner Bailey concluded, "the majority opinion will chill the development of useful comparative price advertising, especially among retail grocers, which is extremely useful to the public, particularly in times of high inflation."

Sections III-VI of this memorandum discuss each of these points in detail. Section III first examines the near-total deference of the courts to the Commission's "expertise" in interpreting ads. Then, section IV explains the nature and operation of a reasonableness standard. Next, section V similarly analyzes the consumer injury requirements. Finally, section VI concludes by discussing the role of FTC cases in actually harming consumers.

Before we begin that anaylsis, however, there is another crucial point to remember. Critics of the proposed statutory change argue that the Commission's law of deception is properly and reasonably defined. Yet examples of past practice show the Commission's staff suggesting that the Commission has sweeping power under the doctrine of deception. The next section explains the staff's belief of the breadth of the deception doctrine.

II. SOME RECENT EXAMPLES OF THE EXPANSIVE SWEEP OF DECEPTION SUGGEST A NEED FOR REDEFINITION

The need for defining "unfairness" is, by now, well recognized. Indeed, the Commission has recommended that Congress define unfairness. But unfairness is only half of our consumer protection mandate. At least with respect to advertising, almost anything that the FTC has ever done, or proposed to do, under its unfairness jurisdiction could be addressed under a deception theory.[4]

Regarding deception, under long-established doctrine, the Commission need only prove that the advertisement has a "tendency or capacity" to deceive.[5] This concept of deception is a standard of considerable breadth. Thus, the staff originally proposed the Children's Advertising rulemaking--the proceeding that demonstrated the breadth of the Commission's unfairness doctrine--on the basis of both unfairness and deception.[6] The initial staff report argued that advertising to young children is inherently deceptive because these children cannot understand the selling purpose of advertising and thus cannot distinguish between ads and programs.[7] Based on this alleged deception as well as on unfairness, the staff proposed that the ads be banned.

Moreover, the Kidvid staff argued that advertising for sugared products failed to mention adverse health effects. This failure, the staff alleged, was also deceptive.[8]

Another example of the sweeping nature of deception involves the staff's recent proposal for rotational warnings to advise consumers on the specific health effects of smoking. The proposed legal basis is that if a significant number of consumers do not know that smoking causes heart attacks,[9] then it is deceptive to advertise cigarettes without disclosing this fact. Yet, the staff's legal theory did not depend on arguing that current advertisements imply that cigarettes are healthful in general, or that they do not specifically cause heart attacks. Indeed, such an argument would seem untenable, given that 90 percent of the population knows of the general health risk of cigarettes, and all cigarette advertising includes a warning.[10] Instead, the staff argued that a significant number of consumers cannot adequately assess the health risk because they do not know the specifics of the risk. If the Commission can, as the staff believes, require cigarette health warnings when there is no evidence that the current advertising deceives anyone, then what could the Commission not do under its deception power?[11]

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[4] The cases in Attachment A illustrate Commission misuse of the deception doctrine in traditional contexts. This section illustrates staff suggestions to expand deception into non-traditional areas.

[5] See, e.g., Charles of the Ritz Distributors Corp. v. FTC, 143 F. 2d 676, 679 (2d Cir. 1944).

[6] FTC Staff Report on Television Advertising to Children (1978).

[7] Id. at 221.

[8] Some believe that the congressional ban on unfairness in rulemaking caused the Commission to end Kidvid. The staff recommendation to end the rule, however, was based on the difficulties of defining which ads would be covered and framing an appropriate remedy, not on the lack of legal basis.

[9] I use heart attacks for illustration. The staff found that other facts needed to be disclosed as well.

Reports and speeches also provide a fruitful source of the staff's views of the near-limitless reach of the Commission's authority under the doctrine of deception. As Section IV of this memorandum discusses, subjective claims should generally be non-actionable: whether or not a subjective claim is accurate depends upon individual perceptions. Yet, in a 1979 report, the Commission staff recommended that the agency give subjective claims "a closer legal scrutiny."[12] Moreover, regarding a Geritol ad with a husband stating "My wife--I think I'll keep her," the number two official in the Bureau of Consumer Protection suggested that a cease and desist order might be appropriate because Geritol could not prove that the use of its product will inevitably generate a state of marital bliss.[13]

It might be suggested that these proposals are irrelevant because they never became law. To the contrary, the fact that high ranking Commission staff have held these views suggests the extent to which deception could be used. True, the Commission never acted on these proposals, but there is little comfort in that fact. Inaction may reflect more the reaction that such proposals provoked in our elected officials of the Congress than any perceived lack of legal authority.

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[10] Staff Report on the Cigarette Advertising Investigation (1981).

[11] I am not addressing the merits of the current proposed legislation, or the merits of such a proposal under an unfairness theory.

[12] Consumer Information Remedies--Policy Review Session (1979) at 150.

[13] Remarks of Tracy Westen, Before the American Marketing Assoc., Aug. 7, 1978.

How, one might ask, has the law of deception reached such a state that some believe that the FTC possess such sweeping power? I turn next to the four problems exemplified by the Kroger, beginning with the Commission's expertise.

III. THE COURTS DEFER TO THE "EXPERTISE" OF THE COMMISSION

The courts have stated that interpreting the meaning of an advertisement is a matter committed to the discretion of the FTC.[14] As former Commissioner Pitofsky concluded, "this modest sounding rule is a principal reason that the Commission has managed to prevail in the appellate courts in the overwhelming majority of its [deception] decisions that have been appealed."[15] Moreover, the Commission can determine the meaning of an advertisement without even sampling public opinion. This attitude is curious. As Ira Millstein, well known trade regulation lawyer, stated:

> The Federal Trade Commissioners themselves are not chosen for their expertise in ascertaining the meaning of advertisements, or for some general intuitive knowledge of the public's understanding of sights and sounds. Of the five present Commissioners, not one has had prior experience in business, let alone advertising. Nor is such expertise invested with the robe. That the Commission's task under the statute is to act in the field of false advertising does not make the Commissioners any more capable of ascertaining the meaning of an advertisement's promise, whatever

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[14] Indeed, as one court put it: "the Commission may 'insist upon the most literal truthfulness' in advertisements ... and should have the discretion, undisturbed by the courts, to insist, if it chooses, 'upon a form of advertising clear enough so that, in the words of the prophet Isaiah, "way faring men, though fools, shall not err therein."'" Charles of the Ritz Distributors Corp. v. FTC, 143 F. 2d 676, 679-80 (2d Cir. 1944). Gulf Oil Corp. v. FTC, 150 F. 2d 106 (5th Cir. 1945); Carter Products, Inc. v. FTC, 323 F.2d 523 (5th Cir. 1963); Doherty, Clifford, Steers & Shenfield, Inc. v. FTC, 392 F. 2d 921, 925 (6th Cir. 1968); J.B. Williams v. FTC, 381 F. 2d 884, 889 (6th Cir. 1967).

[15] Pitofsky, Beyond Nader: Consumer Protection and the Regulation of Advertising, 90 Harvard Law Review 661 (1977) at 667-78.

> the intelligence standard selected, than any other five men (or possibly three), or reviewing court. Rather, courts should occupy in the advertising field the same appellate role they play in reviewing other administrative determinations--no greater perhaps, but certainly no less.[16]

Or, as Commissioner Pitofsky stated:

> Why questions of meaning should be submitted to the virtually unreviewable discretion of five Commissioners of the FTC has never been articulated. Unlike other instances of deference to regulators as part of the administrative process, there is no reason to believe that commissioners of the FTC have unusual capacity or experience in coping with questions of meaning, nor any indication that successful regulation of advertising requires a balance of related regulatory considerations that commissioners are in a special position to handle.[17]

Another recent Commission advertising decision, Ford Motor Co.,[18] illustrates the problems produced by this judicial deference to Commission expertise. The headline of the challenged ad claimed that "all five Ford Motor Company small cars got over 26 m.p.g." The ad stated that mileage varied according to maintenance, equipment, total weight, driving habits, and so forth, and noted that no two drivers or even cars are exactly alike. Despite these disclaimers, the Commission found an implied claim that the average driver would get the advertised mileage. When Ford attempted to use survey evidence to rebut this finding, the Commission did not even think that the surveys raised a sufficient issue of fact to defeat the staff's motion for summary judgment. In short, the Commission brushed aside the survey evidence without even considering it, stating:

> The Commission is not required to survey public opinion to determine what the Ford ads represent to the public; nor is it bound to review

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[16] Millstein, The Federal Trade Commission and False Advertising, 64 Colum. L. Rev. 439, 492-93 (1964) (footnote omitted).

[17] Pitofsky, supra note 15, at 678.

[18] 87 F.T.C. 756 (1976).

> respondent's expert testimony based on survey data, which constitutes a surrogate form of direct consumer testimony.[19]

The Commission's position in Ford leaves no doubt regarding its view of the breadth of its powers to determine the meaning of an ad. Moreover, the Ford decision has precedential effect. Thus, even though there is no reason to believe that the current Commission or staff will misuse this vast discretion, only a change in the law will prevent the meaning of deception from turning principally upon the subjective opinions of three Commissioners.

What would a sound law include? I next consider the two principle elements, discussing first the need to ensure that the Commission focuses only on those claims that reasonable consumers would receive; and, second, on the need to find the likelihood of consumer injury.[20]

IV. THE COMMISSION SHOULD PURSUE ONLY REASONABLE CONSTRUCTIONS OF ADVERTISING.

In general, an act or practice should be deceptive only if it is likely to mislead individuals acting reasonably under the circumstances. As section A explains, a reasonableness restriction is sound policy, ensuring an appropriate focus for the agency's resources and protecting the interests of consumers in the free flow of truthful information. As Section B then details, incorporating a reasonableness restriction into the statute would not impose undue burdens on the agency.

Section B itself is divided into three parts. Part 1 explains how a reasonableness standard would work. It would eliminate some cases, as it should. When Federal Trade Commission action is appropriate, however, it will not be difficult to establish the reasonableness of the Commission's interpretation of the advertising. Nor is there any reason to believe that a reasonableness requirement would lessen protection for vulnerable groups, as Part 2 details. Reasonable children are clearly different from reasonable adults; the Commission should be able to take such differences into account. Moreover, a special exception can and should be included to allow special protection for the vulnerable in those few cases when the reasonableness standard provides inadequate protection. Section B concludes in Part 3 with an analysis of an important subset of claims under a reasonableness standard, namely the common law distinction between factual and opinion claims. As discussed there, it is seldom reasonable to interpret vague, subjective, or obviously exaggerated claims as statements of facts.

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[19] Id. at 794.

[20] In recent years, the courts have shown the first sign of abandoning total deference to the Commision. As attachment A reveals, in two recent case the appellate courts reversed the Commission as to the meaning of the claim. Because both cases involved strained Commission interpretations, however, we cannot rely on them as proof that the courts will establish limits to deception. Even if courts do eventually establish such limits, a judicial definition of deception will emerge only on an ad hoc basis, at considerable expense and time to all concerned.

A. A Reasonableness Standard is Sound Public Policy.

At common law, a claim for deception would lie only for reasonable interpretations of the seller's claim.[21] Because reasonable people would only rely on reasonable constructions of the message, unreasonable interpretations would not be actionable. Of course, what is reasonable depends on the circumstances. The common law applies a stricter standard to evaluate representations when the seller knows those addressed are not reasonable people of ordinary intelligence.[22] Thus, when an advertiser communicates to a vulnerable group, the standard of reasonableness would be a reasonable member of that group.

Two problems exist with challenging messages that reasonable consumers would not find in the ad. First, such cases misuse the FTC's resources. When few consumers misunderstand the claim we challenge, few can be injured; other things equal, we should only pursue claims that are likely to injure reasonable consumers as well as unreasonable ones. By focusing on reasonable constructions of advertising claims, we can achieve more, and more effective, protection for consumers. Second, and more important, pursuing claims understood at most by only a small and unreasonable minority of those exposed to the ad often injures reasonable consumers.[23] When the Commission prohibits an ad based on unreasonable interpretations, it makes it that much harder to communicate truthful and useful information to the larger group of reasonable consumers.

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[21] See W. Prosser, The Law of Torts, § 105 at 684-86 (4th ed. 1971) (discussing how action would lie only for reasonable reliance). Of course, any claim may have more than one reasonable interpretation.

[22] Prosser, The Law of Torts, § 107, at 716-717.

Communication with consumers is a difficult task even without unnecessary obstacles imposed by the Commission. In many instances, firms may have inadequate market incentives to provide information. Information is costly, with firms sometimes unable to recover the costs of providing it. Even when they provide information, firms often find it difficult to attract and hold consumers' attention long enough to communicate the intended message effectively. And, for consumers, locating and processing information are costly activities. When firms have overcome these obstacles and provided useful information to a large audience of reasonable consumers, the circumstances should be extraordinary before we prohibit that communication because of what it might mean to a unreasonable minority.[24]

It is this interest in the free flow of truthful information that has led to the extension of the First Amendment's protection to commercial speech in recent years.[25] Although the Supreme Court has noted an exception for false or deceptive speech from Constitutional protection, it has not yet considered the FTC's approach to deception; nor has it considered the status of a message that informs reasonable consumers, but might mislead unreasonable ones. The current FTC standards were developed when commercial speech was not entitled to Constitutional protection. A standard that requires no likelihood of actual deception, based only on what a minority of unreasonable consumers might believe, as determined solely by the Commission's expertise, may not survive unscathed as the dimensions of Constitutional protection for commercial speech are explored more closely.

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[23] Analyzing some of the claims in Appendix A leads one to wonder if even a trial number of consumers understand the ad in the manner that the Commission asserts. Because the agency need not rely on extrinsic evidence, this question is usually left unanswered.

[24] Again, given the Commission's avoidance of extrinsic evidence, it is significant that the Commission often does not know whether even unreasonable consumers are likely to be deceived.

[25] See Central Hudson Gas & Electric Corp. v. Public Service Comm'n, ___U.S.___, 100 S.Ct. 2343 (1980); Bates v. State Bar of Ariz., 433 U.S. 350 (1977); Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748 (1976).

B. A Reasonableness Standard Would Operate Efficiently.

1. In General, A Reasonableness Standard Poses Few Enforcement Problems.

Deception law appropriately does not provide for a defense based upon the literal truthfulness of the challenged statements. Clever lawyers and advertisers could string together literally true statements, yet make a false inference nearly irresistible. FTC law has gone to the opposite extreme--clever lawyers can take a statement apart piece by piece, looking for every conceivable implication, without regard for whether it is reasonable.

The reasonableness standard is intended to preclude some of this clever lawyering under the current standard that an ad is deceptive if it has the tendency or capacity to deceive. Moreover, a reasonableness standard would sometimes require additional evidence, beyond the Commission's own expertise. Such a standard, however, would not impose any significant barrier in those cases that the Commission should prosecute. It would not require surveys or other extrinsic evidence in all cases; indeed, such evidence would be necessary only in that small class of "close" cases.

In many instances, the meaning of an advertisement to reasonable consumers is likely to be apparent on the face of the advertisement itself. An ad that claims "our product will prevent colds" is going to mean exactly that to most reasonable consumers. Similarly, consider the ad that claims "our product will kill bacteria. Take it when you feel your next cold coming on." Such an ad is likely to lead most reasonable consumers to believe both that bacteria are a significant cause of colds and that the product will prevent colds.

Reasonableness is an ancient and honorable legal doctrine, used by courts and scholars long before reliable public opinion surveys existed. Many areas of law have evolved over the years based on what reasonable people can, and cannot, do under a wide variety of circumstances. Although a different standard from that currently used, reasonable interpretation is thus not likely to be difficult to apply, or will it be foreign to lawyers.

At common law, the meaning of a communication is a question of fact for the jury when statements are capable of multiple interpretations. The jury is asked to assess the significance of the statements to a reasonable person under the circumstances. With a resonableness standard in FTC law, the Commission would be asked to determine those interpretations that reasonable people would place on the challenged ad, given the evidence introduced.[26] In most appropriate cases, the advertisement itself may be the only evidence necessary.

Consider some recent, and I believe appropriate, FTC advertising cases in which we could have determined the meaning of the ads just as easily under a reasonable interpretation standard as under the current standard. In Sears, Roebuck, the Commission interpreted the claims as would reasonable consumers. For instance, the ads claimed:

> No scraping. No pre-rinsing.
>
> It gives you freedom from scraping and pre-rinsing because it has two hot water jets to scour soft food off dishes, and a built-in stainless-steel pulverizer that grinds up leftover food.
>
> With a Kenmore you'll never have to scrape or rinse again. Even dishes crusty with leftover food. Kenmore's 14 powerful hot water jets scour every dish clean ... with no scraping or rinsing.[27]

The administrative law judge granted partial summary judgement on this and other claims with respect to their meaning. Before the Commission, Sears did not challenge the ALJ's finding that it represented that Lady Kenmore would eliminate the need for pre-rinsing or scraping, nor is it apparent how it could have done so under a reasonable interpretation standard. There is simply no other way for a reasonable person to interpret the advertising.

The Listerine mouthwash case is another example in which the Commission gave advertising claims a reasonable interpretation, and in which proof would have been no more difficult under the proposed standard. In that case, the ALJ and the Commission found that the company made claims that Listerine will ameliorate, prevent, and cure colds and sore throats. Some of the claims were:

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[26] Recent Commission and court decisions indicate that the agency is now using a reasonableness standard in determining the meaning of an ad. See Ford Motor Co., 87 F.T.C. 756 (1976); Standard Oil of California v. FTC, 577 F. 2d 653 (9th Cir. 1978); Simeon Management, 87 F.T.C. 1184, 579 F. 2d 1137 (9th Cir. 1978); Sears, Roebuck & Co., 95 F.T.C. 406 (1980), and Kroger Co., D. 9102 (Sept. 25, 1981). Judicial deference to the Commission's expertise limits the significance of this standard, however, particularly in close cases, or where the Commission's interpretation of the ad is not apparent on the face of the ad, as in Ford and in Kroger.

[27] Sears, Roebuck & Co., 95 F.T.C. 406, 416-419 (1980).

> Listerine Antiseptic Kills Germs by Millions on Contact. For Bad Breath, Colds and Resultant Sore Throats.
>
> Fight back with Listerine Antiseptic. Gargle twice a day--starting now--before you get a cold. You may find the colds you do get will be milder; less severe. That's why more people use Listerine during the colds-catching season than any other oral antiseptic.[28]

Unlike Sears, testimony was presented on consumer interpretation of the ads. Although Warner-Lambert conceded it made amelioration claims, the ALJ did consider expert testimony from both sides on the meaning of the ads in terms of prevention and cure claims. It is not apparent how establishing the meaning of the ads to reasonable consumers would have complicated the trial in this case.

On the other hand, there are also recent cases that the proposed reasonableness standard would, and should, have precluded. One recent instance is Kroger, discussed in the Introduction. I find it very difficult to see how the Commission could have argued based only on its own expertise that the interpretation of the ads it challenged was reasonable. Similarly, in Ford, discussed in Section III, how could one argue that the Commission's construction of that advertising was one that reasonable consumers were likely to share? Under the proposed standard, the Commission at least could not have decided the meaning of the ads on a motion for summary judgment; it would have had to consider Ford's survey evidence.

Thus, the reasonableness standard would clarify what is now unclear--the standards by which to judge an act or practice. Both the Commission and businesses would benefit from this increased clarity. The standard would place needed limits on Commission action in those cases when the Commission should not act at all. In cases when the Commission should clearly act, the reasonableness standard would not significantly complicate a trial, it would not require evidence of consumer interpretation, and it would not raise significant problems of application. In cases when it is unclear whether the Commission should act, the standard is likely to require the Commission to develop extrinsic evidence to decide whether to proceed. That is as it should be.

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[28] Warner-Lambert Co., 86 F.T.C. 1398 (1975), aff'd as modified, 562 F. 2d 749 (D.C. Cir. 1977), cert. denied, 435 U.S 950 (1978).

2. A Reasonableness Standard Protects Vulnerable Groups.

Some groups in the population need more protection than reasonable adults. Children are a clear example. Protection of such vulnerable groups is fully consistent with a reasonable interpretation standard. First, reasonableness depends on the circumstances, including the age, sophistication, and vulnerability of the ad's intended audience.[29] Camera angles and photographic techniques that may exaggerate the size or speed of a toy, for example, may mislead the reasonable child, but not the reasonable adult.[30] Similarly, an advertisement that is only relevant to a vulnerable group may be evaluated against the reasonableness of that group. A product that claims to be a miracle cure for terminal cancer victims is not likely to have substantial appeal to other groups, and should be judged against the standards of reasonable interpretation given that the audience is terminally ill. In such a case, there is no policy interest in protecting the interests of reasonable, non-vulnerable consumers, because they have no interest in what the advertiser wishes to convey. The members of the vulnerable groups, however, do have an interest in truthful, useful information about products of particular relevance to them.

Because reasonable interpretations depend on the circumstances, a reasonableness standard will provide ample protection from deceptive advertising that is addressed to a vulnerable group. In other cases, however, vulnerable groups may be part of a larger audience to whom the ad is primarily directed. For example, children may be exposed to advertising intended for adults. Of course, we should not seek to protect children by insuring that all advertising is completely understandable to 4 year olds. On the other hand, in some cases, it is necessary to protect children, and other vulnerable groups, from the consequences of a message that is intended for a larger audience.

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[29] As the Commission noted in Heinz W. Kirchner 63 F.T.C. 1282, 1290; "[a] representation does not become 'false and deceptive' merely because it will be unreasonably misunderstood by an insignificant and unrepresentative segment of the class of persons to whom the representation is addressed. If, however, advertising is aimed at a specially susceptible group of people (e.g., children), its truthfulness must be measured by the impact it will make on them, not others to whom it is not primarily directed." (emphasis added). Too often, the Commission has lost sight of this principle, focusing instead on "vulnerable" groups within a larger audience, at the expense of that larger audience.

[30] Topper, Inc., 79 F.T.C. 681 (1971).

Under the reasonableness test, the Commission will be able to pursue most worthwhile cases involving vulnerable groups. For those few cases in which a "reasonable in the circumstances" test is inadequate, a statutory standard should allow the Commission to challenge ads that would injure vulnerable groups. In such cases, the Commission should be able to challenge advertising if it can show that the advertiser knew or should have known that the ad would mislead some consumers.

In appropriate cases, establishing that an advertiser knew or should have known of the consequences of his advertising should not be a difficult burden to meet. First, "knew or should have known" is not the normal criminal standard. It is much more akin to negligence; indeed, "should have known" is the classic tort phrase for negligence. The Commission need not prove that the advertiser intended the consequences of a particular communication; rather, it is enough to show that the advertiser should have realized the risk that those consequences would follow.

Second, the Commission has developed experience with this standard over the years. Some Commission decisions have applied it in assessing the liability of advertising agencies for false ads. The Commission finds liability by examining objective factors relating to the ad agency's degree of participation in the campaign.[31] Moreover, all of the cases in the defects program except one have pled in the complaints that the manufacturer knew or should have known that the product was likely to experience a particular problem. An investigation considers the information about the problem that was available to the company at the time.[32] Until now, the standard has not been thought to cause an insurmountable, or even a terribly difficult burden.

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[31] Carter Products, Inc. v. FTC, 60 F.T.C. 782 (1962), 323 F.2d 523, 534 (5th Cir. 1963); Doherty, Clifford, Steers, & Shenfield v. FTC, 69 F.T.C. 526, 559, 70 F.T.C. 45 (1966), 392 F.2d 921, 928 (6th Cir. 1968). Other decisions suggest that the ad agency is held to a standard of strict liability. ITT Continental Baking Co., 83 F.T.C. 865, 967-68 (1973), aff'd in part, modified on other grounds, 532 F2d 207 (2d Cir. 1976). See also Porter & Dietsch, Inc. v. FTC, 605 F.2d 294, 309 (7th Cir. 1979), cert. denied, 445 U.S. 950 (1980).

Finally, in many cases, the "knew or should have known" standard will probably not even require additional evidence. It can be argued, for example, that an advertiser should have realized that depicting children riding tricycles into the street could lead some children to believe that this behavior is safe.[33] And, it seems clear that an advertiser should have realized the risk that children would imitate the child in an advertisement playing with a hair dryer near water, particularly because the advertised product was a doll with washable hair.[34]

In short, even with the proposed standard, the Commission will continue to be able to provide valuable protection to vulnerable groups, without a significant increase in the evidentiary burden.[35] By using extreme examples to discourage the enactment of new standards, critics are really suggesting that evidence should not be essential before the Commission acts in cases when it is not clear there has been any wrong to correct. Quite the contrary, I believe that evidence will assure that the Commission acts only when it should.

3. The Law Should Distinguish Facts from Opinions.

The general rule that misstatements of opinion are not actionable at common law rests on the belief that reasonable people will not rely on certain kinds of opinion claims. As Judge Learned Hand stated:

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[32] Chrysler Corp., 96 F.T.C. 134 (1980) (rust); Chrysler Corp., C-3084 (Feb. 17, 1982) (oil filters), American Honda Motor Corp. C-3082 (Jan. 22, 1982), Volkswagen of American Inc., 46 Fed. Reg. 47,617 (Sept. 29, 1981) (provisionally accepted consent). No cases in the defects program have been fully litigated to date.

[33] AMF, Inc., 95 F.T.C. 320 (1980) (consent order).

[34] Mego Int'l, 92 F.T.C. 186 (1978) (consent order).

[35] The Commission can also use an unfairness theory to protect vulnerable groups. Such a theory explicitly requires balancing the benefits of regulation to the particular vulnerable group against the costs to the rest of the population. In cases such as AMF and Mego, this is not likely to be a difficult burden, because correcting the problem will not harm the selling purpose of the ad.

> The reason of the rule lies, we think, in this: There are some kinds of talk which no sensible man takes seriously, and if he does he suffers from his credulity. If we were all scrupulously honest, it would not be so; but, as it is, neither party usually believes what the seller says about his own opinions, and each knows it. Such statements, like the claims of campaign managers before an election, are rather designed to allay the suspicion which would attend their absence than to be understood as having any relation to objective truth. It is quite true that they induce a compliant temper in the buyer, but it is a much more subtle process than through the acceptance of his claims for his wares.[36]

Congress apparently intended to preserve an opinion defense when it added the "unfair or deceptive acts or practices" language to the FTC Act in 1938. Senator Wheeler, one of the bill's sponsors, explained the purpose of the current standard:

> The object of the proposed legislation is not to stop the issuing of exaggerated opinions with reference to one's own articles ....[T]he courts have recognized the difference between simply puffing one's own product in a general statement by saying, for example, "It is the best car manufactured," and misrepresenting a definite fact with reference to the product. If an automobile manufacturer said, "This automobile has a self-starter on it," when as a matter of fact the automobile did not have a self-starter on it, that statement would be a definite, positive misrepresentation of a provable fact. However, if the manufacturer said, "My car is the best car on the market for the money," there would be a vast difference of opinion in the general public's mind as to whether it was or not, and a great many persons might say it was not. It would be a very difficult thing to prove that the car was not just what the manufacturer said it was. Those are things which are generally recognized by the courts as not capable of being reached by any law.[37]

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[36] Vulcan Metals Co. v. Simmons Mfg. Co., 248 F. 853, 856 (2d Cir. 1918).

[37] 80 Cong. Rec. 6592 (1936).

Unfortunately, the Commission has neither applied nor followed this clear articulation of congressional intent. The fundamental difficulty is the Commission's pursuit of interpretations of advertising that reasonable people would not draw. As a result, the agency acts against claims that reasonable people would construe as opinion claims, and would find useful, because some unreasonable consumers might misconstrue the opinion as a fact. Although a puffery defense exists at the FTC, as applied it is much more limited than the common law fact/opinion distinction.

A distinction between facts and opinions is needed. The Commission should not pursue claims about which reasonable persons would disagree if they possessed all the facts, provided that the claim itself gives a fair indication that it is merely opinion. What constitutes a fair indication depends, of course, on the context of the claim. In general, the Commission should not pursue three classes of claims. It should not pursue subjective claims, such as claims about taste or scent. It should not pursue obviously exaggerated claims, such as "put a tiger in your tank." And, it should not pursue correctly stated descriptions of expert opinions, unless there is no reasonable disagreement among experts about the issue. All of these claims are useful to consumers, and seldom, if ever, lead to injury.[38]

Consider first subjective claims. These claims are often essential; there is little way to describe a flavor other than to tell you what I think it is like. Moreover, such claims are virtually always accurate, because they drive some consumers away as well as attract others. For example, the description of a product that "tastes like cola" attracts those who seek colas, and repels those who seek uncolas. Because consumers who seek cola flavor will not return to the uncola falsely advertised as a cola, there is no point in misdescribing the product. The seller who does so ignores his natural market, uncola drinkers, and alienates a market he can never serve in any event.

There are other subjective product attributes that, like taste, cannot be described conveniently and understandably to consumers in a factual way. Contrast power output with handling claims for automobiles. Power output is frequently advertised factually ("200 horsepower") because there is a good and readily understandable measure of this attribute. Handling performance of automobiles, however, is often expressed as opinion, presumably because no simple measurement for it exists. Hence, a seller will opine "handles great" to provide information to consumers. Consumers who are looking for a car with good handling characteristics should consider test driving the advertised car.

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[38] For additional analysis of the economic rationale for the fact/opinion distinction, see Grady, "Regulating Information: Advertising Overview", p. 222-245, in K. Clarkson & T. Muris, The Federal Trade Commission since 1970 (1981).

Opinion claims, in other words, often serve as an invitation for consumers to evaluate the product, not as a claim upon which they should make an irreversible commitment. As already noted, when a claim merely invites search there is a built-in market guarantee of its reliability, because sellers ordinarily do not have an incentive to invite the search of those who especially value a particular characteristic, such as handling, if the product does not actually have it. In this situation, it makes more sense to invite search on some other characteristic, for instance, "roomy backseat."

Of course, there should be a fair indication that it is opinion, as there would be from the claim "handles great". Not only does this claim discuss a subjective attribute (how the car handles), but it is also phrased in an exaggerated way. Hence, such a claim would not be actionable, unless reasonable people in possession of the facts would agree that the car does not "handle great".[39]

As the "handles great" claim indicates, obviously exaggerated statements are also useful. Much of advertising is signaling, indicating that the advertiser believes consumers will like the product.[40] The key to producing such signals is memorable advertising. If obvious exaggerations help consumers to remember the product's name, they reduce the cost of providing the signal. Both consumers and advertisers will benefit. When the Commission challenges such advertising, it reduces the efficiency of what is already a very expensive process.

The common law distinction between facts and opinions, although primarily encompassing the problems of subjective and obviously exaggerated claims, also provides a basis for analyzing expert opinion. The utility of correctly stated expert opinion should be obvious. It allows consumers access to the conclusions of those more knowledgeable than themselves at low cost. For example, it is useful for consumers to know that the Surgeon General has concluded that cigarette smoking is hazardous; or that the American Heart Association has determined that it is prudent to reduce dietary fats and cholesterol; or that Road and Track magazine believes that Vega is the best handling passenger car ever built in the U.S. The Commission, unfortunately, has not always thought so.[41]

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[39] General Motors, discussed in note 41 infra, involved handling.

[40] See Nelson, Information and Consumer Behavior, 78 J. of Political Econ. 311 (1970).

It bears emphasis that this standard would make expert opinion actionable when it is false. For instance, if a noted surgeon opined that cigarettes were good for people, this claim would not fall under the "opinion" category described here, because there is no reasonable disagreement on this point. Those experts in possession of the facts agree that cigarettes have adverse health consequences.

Moreover, a representation of an expert's opinion is a factual claim that the expert holds the advertised opinion. Misrepresentations of expert opinion are clearly subject to challenge even within a distinction between fact and opinion. Similarly, it is quite possible to misrepresent the degree of expertise of the source of an opinion. To advertise the opinion of Nobel Laureate Linus Pauling on the benefits of vitamin C, without disclosing that his prize was for his work in physics, is a factual misrepresentation of the nature of his qualifications. It should be actionable, and is, even if opinion claims are generally excepted from the coverage of the statute.

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[41] As explained in Attachment A, the Commission attacked GM's use of Road and Track magazine. General Motors Corp., 85 F.T.C. 27 (1975) (consent order). There are several problems with this case. "Handling" is a subjective judgment. Indeed, GM's ad stated "there's only one way, really, to find out what a Chevy Vega is all about and that's to drive one." In these circumstances, GM is merely inviting individuals to test a car, not asserting a fact upon which they are meant to rely. Moreover, even if one believes that GM is, on its own, asserting a fact, Road and Track should be adequate substantiation for the claim. Consumers simply could not be deceived into thinking that GM had the substantiation that the Commission required when the actual substantiation-- Road and Track --was stated in the advertisement. To hold otherwise means that consumers are deprived of learning through advertising valuable opinion information from reputable publications. If Road and Track passes the tests discussed in the text for expert opinions --disinterested, accurately represented, etc.--then the claim should be permitted. The Commission did not allege any of these problems.

Further, representation of an expert's opinion implies that the opinion is genuinely held. When the expert's judgement is bought and paid for, this implied representation is false, and actionable. Of course, there is an important, albeit sometimes subtle, difference between paying for an honest opinion and buying the outcome. The latter situation is plainly actionable.

It should also be clear that an advertising claim about the extent of expert opinion is a factual claim. A claim that all experts believe X is actionable if they do not. When a claim uses an expert's opinion in such a way that reasonable consumers would conclude that all experts agree, again there is a misrepresentation of fact that is actionable. This was the situation in the National Commission on Egg Nutrition[42] case, in which the Commission challenged claims that there is "no evidence" linking eggs to heart disease. What is prohibited, however, is misrepresentations about the amount of evidence, not accurate statements of the opinions of various experts.

Finally, and perhaps most importantly, there are significant checks among experts themselves. All an expert has to sell is his judgment. The value of that judgment depends on the expert's reputation. Experts are seldom willing to squander that reputation, because once they do, they have nothing left to sell. To use Commissioner Pertschuk's example, it is inconceivable to me, on the present state of evidence, that Dr. DeBakey could be induced to endorse a cigarette as a cure for cancer. Such an endorsement would destroy his credibility, and marketability, forever.

There remains a core of cases in which legitimate experts will disagree about the "truth" of a claim. It is the nature of such cases that the Commission cannot tell which side is right. When the Commission intervenes in such disputes by prohibiting one side of the debate as "false or deceptive," it will be right only by chance. It seems to me to be the essence of the First Amendment that the government should not impose its own view of such controversies.

V. THE COMMISSION SHOULD ONLY CHALLENGE CLAIMS LIKELY TO CAUSE INJURY

The Commission should only address practices that are likely to injure consumers. There is no reason to spend the taxpayer's resources, or those of the companies whose practices we challenge, except to protect consumers. When consumers are not likely to be injured, they do not need protection. The FTC should challenge only those practices likely to cause an injury that consumers themselves would reasonably regard as significant.[43]

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[42] 88 F.T.C. 89 (1976), enforced in part 570 F. 2d 152 (7th Cir. 1977), cert. denied, 439 U.S. 821 (1978).

The key element of likely injury has been largely eliminated from FTC law. To the extent that the Commission must find that consumers are injured, and few cases require such a finding, the Commission's reliance on its own expertise has emasculated the requirement. A requirement that the Commission in fact prove that this kind of injury is likely before it finds an ad deceptive is not a requirement for quantitative cost-benefit analysis in advertising cases. Nor need injury be measured in monetary terms. Rather, in most instances, a logical inference that injury is likely to exist would suffice, subject, of course, to rebuttal by the respondent's evidence. There are several ways that the Commission could prove the likelihood of injury.

To determine if consumer injury is likely, the key question is whether consumers have to give up something of value if the claim is false. Of course, answering this question directly is difficult. In most instances, however, simpler questions will give reasonable answers, with little need for elaborate evidence.

First, it is unlikely that consumers will give up anything of value unless the product is worth more if the claim is true than it is worth if the claim is false. For example, when an advertiser claims that a product has a certain feature that consumers would like, we can infer that the product is worth more to consumers if the claim is true. Thus, if a dishwasher manufacturer has survey evidence indicating that consumers prefer to avoid the need to rinse dishes first, that would constitute evidence that consumers would find a dishwasher with a no rinse feature worth more than one without it. If there is no other evidence of likely injury, this inference that the product is worth more to consumers is sufficient to justify a finding of injury. The finding of consumer injury would be irresistable with evidence that consumers must pay more for products with the advertised feature. In the dishwasher case, for example, evidence that the price of dishwashers that do not require rinsing is higher than the price of those that do would end debate over the injury issue.[44]

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[43] At common law, this injury test is expressed in the materiality requirement. Materiality has two elements. The consumers must (a) rely on the claim, (b) to their detriment. The statement in the text is another way to express this common law test.

What consumers must forego if the claim is false is not necessarily money, nor need it be reduced to monetary values. Injury exists if consumers forego some other opportunity, valuable in itself, by reason of the deception. Thus, if deceptive advertising induced consumers to drive unnecessarily across town on a Saturday, there could be significant injury in foregone leisure time from the false claim, even if the deception were cured before purchase (as is sometimes the case with bait and switch advertising).

These questions would easily screen out many Commission cases in which there was no injury. In the recycled oil cases,[45] for example, the Commission found no difference in performance between oils refined from virgin crude and those refined from used oil. Given this finding, why would consumers be willing to pay more for oils refined from virgin crude? Nonetheless, the Commission found deceptive the failure to disclose that the oil was recycled. Although the Commission found that consumers preferred the product made from virgin oil, this finding reflected a consumer judgment made with imperfect information. Given their normal experiences, consumers are likely to assume that the difference between new and "used" oil is significant. Given the Commission's finding that it is not, what the consumer evidence reflects is that consumers were asked the wrong question. Instead of protecting consumers, these cases injure them by imposing on consumers the need to gather additional information to determine that a difference that the Commission knows is irrelevant is indeed irrelevant.

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[44] Notice that the price of the advertised product is, in this case, irrelevant. The question is whether the market indicates that consumers generally pay for the advertised feature. Consumers must still forego the chance to purchase a product with the advertised feature, even if the advertised brand is cheaper. In general, price differentials would be the best evidence when available, because they indicate actual, not hypothetical, values for the attribute.

[45] See, e.g., Mohawk Ref. Co., 54 F.T.C. 1071 (1958), 263 F.2d 818 (3rd Cir.) cert. denied, 361 U.S. 814 (1959) see also, Kerran, 54 F.T.C. 1035 (1958), 265 F.2d 246 (10th Cir.), cert. denied, 361 U.S. 818 (1959).

Similarly, a focus on injury would eliminate many of the deceptive pricing cases.[46] These cases involve claims that an advertised price represents a special sale price, or a substantial discount from the "regular" price. The deception involves not the price at which the product is actually sold, which would involve an injury. Rather, the alleged misrepresentations involve the "regular" price, so that the "savings" are misstated.

It is very difficult to see why consumers would pay more for the product even if the "regular" price claim were true.[47] As former Commissioner Pitofsky wrote in criticizing the Commission for bringing such cases, "as long as consumers are accurately informed of the offering price, they can make sensible decisions, and the transactions may still be at prices lower than could be obtained at most other outlets in the marketing area." He further noted that these cases were most frequently brought against discounters, who were attempting to use price as a competitive weapon.[48] Thus, not only did these cases fail to help consumers, they probably injured them.

In assessing injury, an additional question should be asked: can consumers evaluate the claim for themselves at low cost? When they can, they are unlikely to forego anything of significant value if the claim is false. More important, it is extremely unlikely that there will be any deception. When a product is low priced, frequently purchased, and easy to evaluate, there is no incentive to mislead.[49] Although consumers may purchase the product once, they will not do so again. Thus, the returns from a single purchase are unlikely to cover the costs of disseminating the false advertising for a product that meets these conditions. In short, in this class of cases, the market works--deception is not a viable business strategy. In the last few years, the FTC staff, in selecting cases, has used the presence of these three conditions as a reason for not pursuing cases. This attitude is appropriate. In cases like these, consumers are more likely to evaluate the claim accurately than is the Commission. If there is deception, the marketplace is likely to eliminate it before it comes to the Commission's attention.

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[46] See, e.g., Levitz Furniture Corporation, 88 F.T.C. 263 (1976).

[47] In some instances, consumers may use price as an indication of quality. If so, then misrepresenting the regular price misrepresents the quality of the goods, causing injury. What is relevant, however, is the regular market price of the product, not the regular price of this seller. With a well known discounter, such as Levitz, the pricing claims are unlikely to misrepresent quality.

[48] Pitofsky, supra note 15, at 688.

[49] For most such products, what consumers give up is the opportunity to use a different brand of the product. In the Poli-Grip case, discussed infra, most denture wearers probably use some denture adhesive anyway. Thus the injury is the difference in product value, not the price of the advertised brand.

The Commission's opinions have sometimes reflected this point. Thus, in the Dry Ban case,[50] the Commission challenged claims that the product was dry. The complaint alleged that these claims were absolute, meaning that the product was literally dry. The Commission ultimately dismissed the case, because it interpreted the claims as relative claims, in part because the product was inexpensive, frequently purchased, and easy for consumers to evaluate.

Other cases have slipped through, however. A recent example is the case against Block Drug for its advertising of Poli-Grip. These ads claimed that the product would eliminate discomfort and embarrassment when denture wearers ate "problem" foods such as apples. As Commissioner Thompson noted in dissenting from the issuance of the complaint, the product is cheap, purchased frequently, and the claims are easy to evaluate. As he put it, "it is inconceivable to me that any denture wearer who applied Poli-Grip or Super Poli-Grip and bit into a red apple and then saw his dentures smiling back at him would ever purchase the Gripper again."[51]

In other recent cases, in which Commission action was entirely appropriate and justified, the need to establish the likelihood of consumer injury would not have been a significant barrier, and would not have significantly complicated the litigation. For example, consider the recent case against Sears.[52] The company claimed that its dishwasher eliminated the need for scraping and pre-rinsing. Because these are time consuming, undesirable activities, it is reasonable to assume that consumers would be willing to pay more if the claims were true than if they were false.

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[50] Bristol-Myers Co., 85 F.T.C. 688 (1975).

[51] Block Drug Co., 90 F.T.C. 893, 902 (1977) (Thompson, dissenting).

[52] Sears, Roebuck, 95 F.T.C. 406 (1980).

Moreover, in that case, we had survey evidence of injury. A market survey conducted by Sears indicated that a large segment of the public wanted a dishwasher that eliminated the need for pre-scraping and pre-rinsing, and were willing to pay more for this feature. The ability of a dishwasher to clean dishes on the upper rack was also an important factor to the public, as was the ability of a dishwasher to clean pots and pans.[53] Thus, had the claim been true, consumers apparently would have been willing to pay a premium for the product. Moreover, the cleaning performance claims are clearly ones the consumer cannot evaluate without incurring a large expenditure.

Another example of a recent case protecting consumers from injury is Listerine.[54] The company claimed that the product would prevent colds or lessen their severity. It can be inferred that consumers would have been willing to pay some increment more for Listerine if the claims had been true. Certainly, anyone who has suffered the common cold is likely to be willing to pay at least some amount of money to ameliorate or prevent the cold. There was also survey evidence indicating that many consumers thought fighting colds was an extremely important characteristic of a mouthwash. Further, it was difficult for the consumer to evaluate the accuracy of these false claims because most colds are self-limiting and improve without medication.[55] Again it is difficult to see how an injury test would have significantly complicated this litigation.

Of course, a consumer injury test would eliminate certain cases that I believe should not be brought. It would not, however, substantially complicate those cases when the Commission should clearly act. When it is not clear whether the Commission should act, it would be necessary to consider external evidence before deciding which course is appropriate, rather than relying on introspection. When appropriate policy is not clear, more evidence is likely to lead to better decisions.

VI. CONCLUSION: A NEW DECEPTION STANDARD WILL HELP THE AGENCY AND CONSUMERS.

Because the current Section 5 legal standard is so broad and ambiguous, case selection has been a time-consuming and recurrent problem. Because the Commission can do almost anything, the question has always been what should it do? Ideally, a body of law should clearly characterize a central core of transactions that will always result in liability. The cases at the fringe should possess many of the characteristics of those cases within the core but present a difficult issue of fact or proof on an identifiable characteristic. For instance, in a district attorney's office, the evaluation of a murder case might focus on whether an accused was acting in self-defense. All persons in the DA's office would share a common understanding of what makes a case strong and what makes a case weak. No such shared understanding exists at the FTC. Several consequences follow from this absence of shared understanding of the difference between a strong case and a weak case:

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[53] Id. at 491.

[54] Warner-Lambert Co., 86 F.T.C. 1398 (1975).

[55] See Id. at 1462.

- Enforcement tends to be faddish;
- The attorneys at the investigative level will predictably waste time and resources investigating cases that they believe to be strong but their superiors believe to be weak (as at the end of an enforcement "fad");
- Much time and many resources are lost in the evaluation process to distinguish strong cases from weak cases.

The proposed standard should result in a considerable reduction in the complexity of the case selection process by increasing the level of shared understanding of what distinguishes a good case from a bad case. The proposed standard clearly specifies a central core of strong cases, viz., claims that, when reasonably construed, misrepresent a fact that is likely to induce significant injury. For cases at the fringe of this core, there may be disagreement within the agency about what a reasonable construction of the advertisement would be, about whether it involved a representation of fact, and about whether significant injury is likely. Such disagreements would be far more focused than those that exist currently.

There is a more important problem of our law of deception. As I have tried to indicate, not only have many of the Commission's cases not helped consumers, but they have in fact probably harmed consumers. When the Commission pursues unreasonable interpretations of advertising claims, it increases the difficulty of communicating to reasonable viewers, who understand the claim as intended. When it pursues claims that lead to no injury, it needlessly interferes with the complex and imperfectly understood process of communication, with no offsetting benefits.

Consider Kroger. Comparative price advertising provides consumers with useful information. Such information helps consumers to locate lower priced stores, stimulating all stores to lower prices. Kroger, it is true, did not absolutely prohibit such information. However, it made comparative price advertising more costly, more difficult, and therefore, less likely. In fact, Kroger halted its Price Patrol advertising, even though the Commission conceeded Kroger's basis argument that its prices were frequently below or equal to those of its competitors. Until this decision is reversed, it is only a bold advertiser indeed who will attempt similar advertising. Commissioner Bailey's fear that the decision will similarly chill other comparative price advertising will likely be the reality.

Consider Ford. This case occurred before EPA measured gas mileage. Consumers were quite interested in gas mileage, yet reliable information was not available. When Ford's carefully qualified ads provided such information, the Commission prohibited them as deceptive. This Commission action delayed the availability of mileage information, even though the market was willing to provide it. There is a legitimate role for the Commission in preventing deceptive tests that purport to prove what they do not, but this was hardly the situation in Ford. Ford only discouraged the provision of useful information to consumers.

Consider General Motors. In this case, the Commission prohibited a claim that Road and Track magazine found Vega the best handling car ever built in the U.S. The Commisson told GM that it could only discuss the handling superiority of Vega if it relied upon elaborate scientific testing. Thus, consumers are barred from receiving valuable opinion evidence from a reputable publication.

Finally, consider the fictitious pricing cases. The Commission has most often pursued these claims against discounters. As former Commissioner Pitofsky noted, such cases make it more difficult for discount outlets to convey their advantages to consumers.[56] Again, the Commission has surely not benefited consumers, and may have injured them.

One can find numerous other examples of consumer injury, both recent and more distant, in the uneven history of FTC deception law. To avoid such examples in the future, the agency must be directed to focus on only those ad claims that reasonable consumers would understand and on likely consumer injury. These standards are well-known to lawyers from the common law, and thus can be easily transferred to the FTC.

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[56] Pitofsky, supra note 151 at 688.

Throughout its controversial 68 year history, the FTC has never quite fulfilled its promise of providing consistent and substantial protection to consumers. The fault lies not in the fine people who have served here, but instead in the overly broad standards that Congress has provided us--standards that do not provide guidance on how to proceed. With these broad standards, in one era the Commission did little, focusing largely on trivia. In the next, the Commission took upon itself the mantle of the second most powerful legislature in America, surely a task inappropriate for five unelected officials.

With a Congressional definition of deception--and of unfairness--the Commission can, and will, enter a new era. We will have a defined and obtainable mandate: protection of consumers from those serious deceptive and unfair acts and practices that still plague us today. And the public whom we serve, as well as regulate, will have a greater understanding of what the law is.

Attachment A

CASES RELIED UPON BY CHAIRMAN MILLER FOR HIS TESTIMONY

This list is not exhaustive. It includes some cases from before the 1970's, because they indicate the wide discretion available to the Commission in its consideration of the deceptiveness of a particular claim.

CLAIMS ON WHICH THE COMMISSION PREVAILED

Kroger Co., D. 9102 (9/25/81)

Kroger's advertising described the results of its "Price Patrol," in which homemakers surveyed prices of 100 to 150 items at local supermarkets. The Commission conceded "that the evidence does not dispute Kroger's basic argument that its prices were frequently below or equal to those of its competitors." Nevertheless, based on its own expertise, without any other evidence of the ad's meaning, the Commission held that the ads were deceptive because they implicitly represented that the surveys were "methodologically sound" and "statistically projectible."

Commissioner Patricia Bailey dissented on the meaning of the ads. She noted that Kroger made a point of emphasizing the informality of the surveys. She wrote, "the notion that these surveys were 'methodologically sound' and therefore 'prove' an overall 'projection' of lower prices is simply, in my view, an artificial construct imposed by the majority [of the Commissioners] on the ads in question." On the merits of bringing this case, she wrote, "I fear that the majority opinion will chill the development of useful comparative price advertising, especially among retail grocers, which is extremely useful to the public, particularly in times of high inflation." This case is currently on appeal.

Block Drug Company, 90 F.T.C. 893 (1977)

The FTC challenged claims that Poli-Grip would help denture wearers eat problem foods, such as apples, without discomfort or embarrassment. This product is cheap, frequently purchased, and easy for consumers to evaluate for themselves. When these three facts are present, the FTC is not needed to police the marketplace, because advertisers cannot make enough money from deception to recoup their investment in the advertising. As Commissioner Mayo Thompson said in his dissent, "it is inconceivable to me that any denture wearer who applied Poli-Grip or Super Poli-Grip and bit into a red apple and then saw his dentures smiling back at him would ever purchase the Gripper again."

Ford Motor Co., 87 F.T.C. 756 (1976)

The headline of the challenged ad claimed that "All 5 Ford Motor Co. small cars got over 26 mpg." The ads stated that mileage varies according to maintenance, equipment, total weight, driving habits, and so forth, and added that no two drivers, or even cars, are exactly alike. Despite these disclaimers, the Commission found an implied claim that the average driver would get the advertised mileage. The Commission found this claim based solely on its own expertise, and without considering a survey conducted by Ford.

Levitz Furniture Corporation, 88 F.T.C. 263 (1976)

A discount furniture store ran ads that claimed "New Reduced Prices," and "Levitz Furniture actually lowers prices." The Commission alleged that the ads claimed consumers would save from Levitz's regular price. As former Commissioner Pitofsky wrote in criticizing the Commission for bringing these fictitious pricing cases, "as long as consumers are accurately informed of the offering price, they can make sensible decisions, and the transactions may still be at prices lower than could be obtained at most other outlets in the marketing area." 90 Harvard Law Review 661 (1977) at 688.

Nagle, Spillman & Bergman, Inc., 88 F.T.C. 244 (1976), and Morton-Norwich Products, Inc., 86 F.T.C. 299 (1975)

In these cases, the Commission challenged claims for two salt substitutes. Both companies claimed that their products, substituting potassium chloride for sodium chloride, were appropriate for those who wanted to decrease their salt intake. None of the ads mentioned potassium. Nonetheless, the Commission found that the ads were deceptive because they failed to mention that the product should not be used by those on a potassium-restricted diet.

In Nagle, the Commission also challenged a claim that the product "tastes like salt." Not only is this claim inherently subjective, but because the product is cheap and frequently purchased, consumers can easily evaluate whether it tastes like salt.

General Motors Corp., 85 F.T.C. 17 (1975)

GM advertised that Road and Track magazine found the Vega to be the best handling passenger car ever built in the U.S. The Commission interpreted GM's claim to mean that Vega really is the best handling car. Because the Commission apparently felt that Road and Track magazine was not adequate substantiation, GM could not substantiate the broader claim the Commission inferred from the ad. The result of the order in this case is that consumers are deprived of learning through advertising valuable opinion information from reputable publications.

Spiegel, Inc., 82 F.T.C. 20 (1973), 494 F.2d 59 (7th Cir. 1974), cert denied, 419 U.S. 896 (1974)

In its advertising circulars, Spiegel offered products on 30 days "free trial" or at a "percentage off." These offers were subject to the customer meeting credit qualifications, a requirement mentioned only in small print and stated in the Spiegel catalogue. Spiegel required the customer to submit credit-related data with the order. The Commission, over the dissent of Commissioner Miles Kirkpatrick, concluded that the ads created the impression that the offer was unconditional when actually it depended on the customer's credit rating. When the appellate court upheld the Commission, Judge Pell, in dissent, wrote that the Commission had found "a detriment to the public interest in the situation of deadbeats being deceived into thinking they are going to receive a free trial of, or discount on, merchandise which they could not realistically purchase on either a cash or a deferred basis."

Brite Mfg. Co., 65 F.T.C. 1067 (1964), 347 F.2d 477 (D.C. Cir. 1965)

Brite involved watch bands that were imported largely from Japan, and so marked on the back. Based on its own expertise, the Commission found that there was a preference among Americans for domestic watches and that it was deceptive to fail to disclose the foreign origin of the watches prior to sale.

Dannon Milk Products, Inc., 61 F.T.C. 840 (1962)

Dannon's advertising described yogurt as "Nature's perfect food that science made better." Although Dannon argued that this was mere puffing, the Commission found that the claim that a food is perfect "concerns nutrition," and is therefore a factual claim. The Commission challenged this claim because a person could not subsist on a diet of yogurt alone.

Mohawk Ref. Co., 54 F.T.C. 1071 (1958), 263 F.2d 818 (3rd Cir. 1959), see also, Kerron, 54 F.T.C. 1035 (1958), 265 F.2d 246 (10th Cir. 1959)

The point-of-purchase materials and labels did not make any claims alleged to be false, but they failed to disclose that the oil being sold was refined from previously used oil rather than virgin crude oil. Although the evidence showed that re-refined oil was as satisfactory for lubrication as virgin crude oil, the Commission held that the failure to disclose that the oil was re-refined was deceptive.

Liggett & Myers Tobacco Co., 55 F.T.C. 354 (1958)

In this case, a cigarette company claimed that its product had a taste that was "always milder." The hearing examiner dismissed this charge as mere puffing and said that there was no public interest in litigating the case. The Commission reversed and found that in the context of the ad, the "milder" claim suggested that it was less irritating in a physical sense, and, not just milder to taste or smell. Under either interpretation, consumers can determine for themselves whether this cigarette is milder.

Gelb, 33 F.T.C. 1450 (1941), aff'd as modified, 144 F.2d 580 (2d Cir. 1944)

The Commission sued a manufacturer that claimed its hair coloring product was permanent because it was feared that some consumers might believe it would color hair that had not yet grown out. The Court of Appeals noted that "it seems scarcely possible that any user of the preparation could be so credulous as to suppose that hair not yet grown out would be so colored." Nonetheless, it upheld the Commission's order.

Sebrone Co., 34 F.T.C. 1126 (1942), aff'd 135 F.2d 676 (7th Cir. 1943)

A deodorant that claimed to "kill strongest odors" was challenged as false by the Commission because it only masked, and did not destroy, odors. Deodorants are an inexpensive, frequently purchased product, and consumers can easily determine for themselves whether they are satisfied with the product.

CLAIMS ON WHICH THE COMMISSION LOST ON APPEAL

The courts have frequently stated that the meaning of an ad is a matter committed to the discretion of the Commission. As former Commissioner Pitofsky wrote, "this modest sounding rule is a principal reason that the Commission has managed to prevail in the appellate courts in the overwhelming majority of its [advertising] decisions that have been appealed." 90 Harvard Law Review 661 (1977) at 667-78.

The following cases provide a welcome sign that the courts are no longer deferring to the Commission completely. Nonetheless, it is not at all clear that the courts will impose a significant check regarding deception. Even if they do, constraints will emerge only on an ad hoc basis, at considerable expense and time to all concerned.

Standard Oil Co. of California, 84 F.T.C. 1401 (1974), modified 577 F.2d 653 (9th Cir. 1978)

This case involved claims that a gasoline additive, F-310, would reduce air pollution. The Commission interpreted a visual demonstration, featuring black smoke from a car's exhaust without F-310 added, then clear exhaust after F-310 was used, as a claim that the additive would "cause the disappearance of virtually 100 percent of exhaust emission pollutants." The Court of Appeals reversed this finding, stating "we do not think that any television viewer would have a level of credulity so primitive that he could expect to breathe fresh air if he stuck his head into a bag inflated by exhaust, no matter how clean it looked."

Trans World Accounts, Inc., 90 F.T.C. 350 (1977), modified, 94 F.T.C. 141, further modified, 94 F.T.C. 1051, aff'd in part and remanded in part 594 F.2d 212 (9th Cir. 1979)

This case involved letters sent by a debt collection agency urging immediate payment and stating failure to comply may result in immediate commencement of litigation by our client." The Commission found that the letters were deceptive because they threatened imminent legal action when no such action was contemplated. Commissioner Collier dissented, writing that "may" means legal action is possible, not probable. He noted, "[t]he majority's decision effectively regulates the word 'may' out of respondents' vocabulary." The Court upheld the finding of liability, but reversed the Commission's restrictions on the use of the word "may."

CLAIMS ON WHICH THE COMMISSION DISAGREED WITH THE STAFF

In these cases, the Commission issued a complaint that was later rejected either by an administrative law judge, or by the Commission itself on appeal. Although the staff ultimately did not prevail, the mere fact that the Commission thought there was reason to issue a complaint illustrates the current problems with the deception standard. Tens of thousands of dollars were spent regarding these complaints -- in the case of the Children's Advertising rulemaking, which was based on both unfairness and deception, over $1,000,000 -- that would not have been spent had a better statutory definition of deception existed.

California Milk Producers Advisory Board, 94 F.T.C. 429 (1979)

The complaint challenged an advertising slogan that "every body needs milk." The Commission, in issuing the complaint, interpreted the claim to mean that milk is essential for all individuals, even those who are allergic to milk, and that it is beneficial in large and unlimited quantities. The administrative law judge agreed with the interpretation of the ads, but concluded that since less than one percent of the population was allergic to milk, there was no public interest in proceeding.

Jay Norris, 91 F.T.C. 751 (1978), aff'd as modified 598 F.2d 1244 (2d Cir. 1979)

One of the claims the Commission challenged was the claim that nylon socks were "guaranteed to wear forever in normal use." The complaint alleged that these claims meant that the socks were literally indestructible and would last forever. The Administrative Law Judge dismissed this allegation. He held that the ad claimed that the socks would last a long time, and that if they wore out, Jay Norris would replace them. This portion of the decision was not appealed to the Commission.

Bristol-Myers Co., 85 F.T.C. 688 (1975)

The complaint in this case challenged advertisements that depicted Dry Ban as clear and dry when it was applied, in contrast to another leading brand, that was oily and sticky. The complaint interpreted these ads to mean that Dry Ban was "a dry spray that is not wet when applied to the body." On appeal from the administrative law judge's initial decision upholding the charges, the Commission concluded that the ads claimed only that the product was drier than competing brands. The Commission dismissed the complaint. As Commissioner Mayo Thompson noted in his concurring opinion, "[i]f the American consumer has no more serious problem than the possibility of being deceived as to the relative 'dryness' of his underarm deodorant, he is in much better shape than I had been led to suppose at the time I joined this agency."

Firestone Tire and Rubber Co., 81 F.T.C. 398, *aff'd* 481 F.2d 246 (6th Cir. 1973)

The Commission's complaint alleged, among other things, that the tire name "Safety Champion" implied that these tires were safer than all other tires. A consumer survey conducted by the company showed that only 1.4 percent would perceive the claim alleged in this complaint. Nonetheless, the ALJ enjoined the use of the term because he interpreted it as representing that the tires were free from defects and safe under all conditions of use. The Commission reversed the prohibition against the use of the term, finding that "Safety Champion" does not represent that the tire is safer than all other tires.

ATTACHMENT 2

Section 5(m)(1)(B) Projects

(1) The Toy Industry

In January 1976, the Commission approved a synopsis to be served on the toy industry. The investigation focused on misrepresentations of the performance of toys in advertising or packaging and on pictures which created a false impression of the toys. Sixty synopses were mailed to selected members of the industry, three cases were developed, and two consent judgements totalling $140,000 were obtained. The determination of law set forth in the synopses were relatively general, e.g., "It is an unfair and deceptive act or practice to misrepresent the performance of a toy." Thus, the synopses were most effective as a predicate for civil penalties where staff could establish clearcut cases of performance misrepresentations. Staff concluded, however, that general determination synopses create serious problems in showing the defendant in a Section 5(m)(1)(B) action had the requisite actual knowledge that what it was doing is unfair or deceptive. Therefore, we have not used this synopsis for some time.

(2) The Textile, Wool and Fur Industries

These synopses have been used to gain compliance with Commission decisions under the FTC Act and Textile, Wool and Fur Acts. In October 1976 they were served on 175 members of the textile products industry. In July 1978 synopses were served on 60 members of the fur products industry and over 110 firms have now been served. Follow-up subpoenas were not needed because staff made on-site inspections to determine the level of compliance. Four consent judgments were obtained involving violations of the Wool and Textile Acts and resulted in a total of $80,000 in civil penalties. A fifth consent judgment is before the Commission.

(3) The Birmingham Home Improvement Industry

This Section 5(m)(1)(B) project involved home improvement contractors located in Birmingham, Alabama. 40 synopses were served and five cases initiated. Those synopses sent were the Advertising And Sale of Home Improvement Products and Truth-in-Lending Act's Right of Recission in Certain Consumer Credit Transactions. The relatively small size of the companies and the transient nature of their principals had a limiting impact on the number of cases developed and on the amount of the civil penalties contained in the proferred consent judgments. Four consent judgments for a total of $40,000 in civil penalties have been obtained.

(4) The Home Insulation Industry

Since November 1977, over 1200 members of the home insulation industry, which consists of manufacturers of mineral wool products, cellulose, urea based foam, cellular plastics products, and aluminum foil have been served with synopses. The 3 synopses were: Energy Savings Claims, Reasonable Basis for Product Claims, and Safety Risks of Products. Two stipulated injunctions, i.e., Kettle Moraine Electric and ATI Northwest Insulation Co., were obtained. The staff believes that this Section 5(m)(1)(B) project has had a substantial and beneficial impact on the conduct of the industry.

(5) Unordered Merchandise

This Section 5(m)(1)(B) project is primarily used to obtain compliance with the Unordered Merchandise Statute -- 39 U.S.C. Section 3009. It is also used to educate consumers of their rights under the Statute and existing case law. Over 200 synopses have been sent to distributors of unordered merchandise (as a result of complaints received by the Commission) during the last two years. Approximately 15 companies were subsequently served with subpoenas for further investigation and analysis. Since the inception of the Project, in 1979, two cases have been fully developed. This relatively small number of cases is attributable to several factors: (1) the small size of the companies, (2) the transient nature of the companies and principals, and/or (3) general compliance after having received the synopsis. A consent civil penalty judgment was obtained in Sure Products, Inc. and Marvin Saline Cir. Action No. 81-0717 U.S. District Court, District of Columbia (1981). In Sure the Decree provided for $30,000 in civil penalties and a broad injunction.

(6) Business Opportunities

This synopsis was approved in September 1975, revised in April 1977 and again in December 1978. In the last 3 years the synopsis has been sent out to over 1400 entities consisting of franchisors and those on the periphery of Trade Regulation Rule coverage. Generally it is sent with a copy of the Franchise Rule. One civil penalty case has been developed and several other cases are under consideration.

(7) Housing Industry - Consumer Credit Advertising

This synopsis has been sent to 73 firms in the last 3 years. These firms were located in areas served by Atlanta, Boston, Dallas and Chicago Regional Offices. Additionally, synopses were sent by headquarters to companies on a nationwide basis. 13 civil penalty cases have been developed to date. The penalties ranged from $10,000 (Downing Associates) to $90,000 (U.S. Home Corp.). The majority of the cases (10) were settled in the $25,000 to $50,000 range.

(8) Rescission Rights in Consumer Credit Transactions

This is a Dallas Regional Office project in which 10 firms have received the synopsis notifying them that the Truth-in-Lending Act requires notice of the right to rescission in certain consumer credit transactions. Firms served have been home improvement companies, realtors and automobile dealers. One case is still active and civil penalty action against a home improvement dealer may be forthcoming.

(9) Sale of Credit Life of Accident & Health Insurance in Connection with the Consummantion of a Consumer Credit Transaction.

These synopses were served by the New York and Chicago Regional Offices and headquarters. The major issue has been whether the FTC has jurisdiction over insurance companies.

(10) Credit Balances on Retail Consumer Charge Accounts

A synopsis was served on Zale Corp. as part of an investigation of that company. It has not been used other than on Zale in the last three years. The synopsis was helpful in obtaining a broad FTC consent order (not court judgment) against the firm.

(11) Disclosure of the Filling Contents of Feather and Down Products

This is a Denver Regional Office project in which 344 manufacturers, marketers, sellers and advertisers received the synopsis. It has resulted in two civil penalty actions being filed. Another case is being developed for civil penalties. The project has increased Commission visibility in the industry.

(12) Magazine Subscriptions - Recruitment of Employees and Sales

Two firms received synopses in the last 3 years. Union Circulation is in litigation in district court. The other firm is currently being investigated.

(13) Sales of Merchandise or Services

The Door-to-Door Sales of Encyclopedia synopsis was originally approved in February 1976. The Dallas Regional Office sent out 4 notices under the original synopsis. This synopsis was revised to Sales of Merchandise or Services on June 26, 1978. The Cleveland Regional Office sent 884 revised synopses to Kirby vacuum cleaner dealers, a national door-to-door seller. One civil penalty case has been approved by the FTC but not yet filed in court.

(14) Vacation Promotions

This was developed as part of a 1980 projet against unnamed vacation award promoters. The project has resulted in one injunction (Harbor Village) and one civil penalty recommendation currently before the Evaluation Committee.

(15) Debt Collection Practices

The synopsis was approved September 23, 1975. Five synopses have been sent out in the last 3 years and since then 3 cases have been developed and subpoenas have been served. There have been no complaints concerning this synopsis, however, it was not widely used since the Fair Debt Collection Practices Act went into effect.

(16) Hair Loss or Baldness Treatments - Advertising

This synopsis was first approved on June 26, 1979. Two synopses have been sent and since then, 2 cases have been developed; one of them is now in District Court.

(17) Idea and Promotion and Marketing Practices

This synopsis was sent to one company which willingly complied with it. Therefore, this case did not result in a lawsuit.

(18) Presale and Availability of Warranty Terms

This synopsis was approved November 7, 1979. In the last 3 years, the synopsis has been sent to 32 merchandisers representing 6 chains and 17 national retailers. No cases were developed although National Merchants Retailer Institute filed a petition to revise the synopsis. This petition is still pending.

(19) Fair Credit Reporting

This synopsis was approved February 8, 1977.

(20) Denture Adhesive and Cleanser Products

After approval on May 17, 1979, 5 companies were sent this synopsis in the last 3 years. No cases have been developed.

(21) Freezer Meats - Advertising and Sales

This synopsis was originally approved September 23, 1975 and was revised June 27, 1978. In the last 3 years, one has been sent to Jim Clark's Beef Co. This case is still in litigation.

(22) Disclosure of Health and Safety Risks and Treatment Inefficacy

This synopsis was approved on March 26, 1979. The Cleveland Regional Office sent out 21 synopses to regional weight loss clinics, who included the use of the drug HCG in their programs. Although 4 subpoenas were issued, no cases developed because staff determined that the clinics had complied with the synopsis. The program was viewed by the staff as very successful because companies willingly complied with the synopsis.

THE COMMISSION HAS ALSO APPROVED THE FOLLOWING SYNOPSES BUT THEY HAVE NOT BEEN SENT TO ANY FIRM IN THE LAST 3 YEARS

(23) Wait and Switch Sales Practices

(24) Automobile Rental Practices

(25) Sale of Used and/or Rebuilt Merchandise

(26) Sale of Merchandise Which is Damaged or Defective or Defective or Different From That Ordered

(27) Demonstrations

(28) Endorsement and Testimonials

(29) Substantiation of Product Claims

(30) Retail Food and Grocery Merchandising Practices Advertising and Marketing Practices

(31) Cosmetics - Advertising and Sale

(32) Tires - Advertising and Sale

(33) Recruitment of Employees and the Sale of Magazine Subscriptions

(34) Use of Presciption Drugs Not Approved by the Food and Drug Administration for Treatment of Obesity or Weight Control

(35) Advertising of Drugs Determined by the Food and Drug Administration to Not be Generally Recognized as Safe and Effective for the Use for Which They are Advertised

(36) Any Imitation Numismatic Item - Hobby Protection Act.

(ix) Senator KASTEN. The committee will come to order. This panel consists of Mr. James P. Carty, Mr. Jared Blum and Mr. Roland Brandel. Our first witness on the panel is Mr. Carty, whom I understand is accompanied by Mr. Howard Vine. Mr. Carty is representing the National Association of Manufacturers. I understand that you have a prepared statement. We would like for you to limit your remarks at this time to approximately 5 minutes.

What we will do is we will go through the entire panel, and then address questions from the committee to any and all of you. Mr. Carty.

STATEMENTS OF JAMES P. CARTY, NATIONAL ASSOCIATION OF MANUFACTURERS, ACCOMPANIED BY HOWARD VINE, DIRECTOR OF CORPORATE GOVERNANCE AND COMPETITION COMMITTEE; JARED BLUM, SMALL BUSINESS LEGISLATIVE COUNCIL; AND ROLAND BRANDEL, CONSUMER BANKERS ASSOCIATION

Mr. CARTY. Thank you, Mr. Chairman. I look forward to working with you and other members of the committee on the 1982-83 FTC authorization.

NAM members are highly sensitive to the impact of FTC actions upon their businesses, both from the perspective of the Commission's antitrust or unfair methods jurisdiction and the Commission's prohibitions of unfair or deceptive acts or practices. NAM members view the reauthorization process as a significant opportunity to reexamine areas in FTC practices needing refinements.

The fact that the FTC remains on a short swing reauthorization process of a 2-year cycle allows constituents of the agencies including the NAM the opportunity to bring before Congress relevant information relating to the success or failure of the agency in handling its mission.

The NAM views Federal intervention through the FTC or other agency action as a course which should be pursued with caution. The vast power and resources of the Federal Government should be reserved for those cases where statutory policy guidance is explicit. Substantial injury is likely to occur and could not be reasonably avoided, and the cost of the injury has a net effect which outweigh the overriding benefits to consumers or competition.

NAM specifically urges this committee and the Congress during this reauthorization process to focus upon the elements which form the basis for prosecutorial and rulemaking discretion of the FTC. Further, the NAM suggests that Congress employ this authorization process to channel the resources of the Commission and to enunciate with clarity the basis both for Federal intervention and the imposition of penalties which will be consistent with policies that seek to accomplish deterrence, punishment and compensation.

For a moment, turning to unfair methods of competition, the NAM has deferred comment on that portion of the FTC Act dealing with antitrust matters during this reauthorization hearing. This by no means should be construed as NAM's acquiescence to the present formulation, interpretation and application of that jurisdiction.

By separating out this issue; that is, the unfair acts and practices and the unfair methods, during this authorization hearings, the NAM urges that Congress soon—and I underline soon—return to consider the enforcement ramifications of the present application of unfair methods. Such a focus on unfair methods jurisdiction should closely follow Congress resolution of the definitional and prosecutorial difficulties inherent in the application of unfair acts or practices.

Turning to the unfair acts or practices section, the issue of greatest concern to our membership at this time stems from the ability of the Commission under section 5(a)(1) to challenge conduct on the basis of a prohibition of unfair or deceptive. The NAM membership has struggled to define the meaning of the term. As you know, the legislative history accompanying Congress enactment of the unfairness provision provides little guidance for the purposes of aid compliance. As a result, the NAM is certain that without congressional input at this time on the elements that form the basis for Commission actions, neither reliance or clarity will be reflected in future FTC actions.

The NAM is confident that the past problems that have befallen the FTC and its constituents, needless prosecutions, improper allocation of resources, and vast expenditures of dollars, can be avoided through codification of prosecutorial and rulemaking tests. The tests which the FTC endorsed and which we support are embodied in the March 5 Commission letter to the Senate Commerce Committee.

NAM supports the recommendations of the FTC for prosecutorial test elements, which are composed of three elements: Foreseeable substantial consumer injury, inability of consumers to reasonably avoid such injury, and the conduct in question is not outweighed by the countervailing benefits or costs.

Actions should be premised solely on the establishment of each criterion. Failure to substantiate a basis of action because one element may be lacking would serve to prevent any FTC involvement.

Turning to the element tests, substantial consumer injury—the Commission would be required to show on the record that the actual injury at issue could reasonably have been foreseen, that the injury must be of such substantial nature as to plainly justify Federal intervention.

As the Commission stated in its December 17, 1980, letter to the committee: "* * * emotional impact and other more subjective types of harm will not ordinarily make a practice unfair. Thus, for example, the Commission will not seek to ban an advertisement merely because it offends the taste or social beliefs of some viewers."

The NAM fully agrees. We urge Congress to follow the Commission's most recent elaboration of March 5, 1982, on the meaning of substantial consumer injury wherein the Commission stated: "As a general proposition substantial injury involves economic or monetary harm and does not cover subjective examples of harm such as emotional distress or offense to taste or social belief."

Avoidability of consumer injury, the second part of the test—the NAM also supports the Commission on its definition of avoidable consumer injury. In the March 5 letter, the Commission said:

> An unfair act or practice must be one which consumers could not reasonably have avoided. The commission should not be involved in rectifying the unfortunate choice of a particular consumer decision. It should confine its activities to curb behavior that takes unfair advantage of consumers' inadequate knowledge in reaching a decision or inability to protect themselves from such behavior.

The FTC position supported by the NAM is no retreat to the old days of caveat emptor. Under the reasonably avoidable standard of section 5, the act would continue to reach abusive conduct which distorts or frustrates free consumer choices. Examples would include the selling of phony cures to seriously ill cancer patients, refusing to reassemble appliances supposedly dismantled for inspection until a contract is signed, et cetera.

Turning to the countervailing benefits test, the determination of countervailing benefits will force a matter in question to be fully balanced between the potential harmful act or practice and the net practical benefit to consumers or competition.

I see my time has expired.

Senator KASTEN. If you could just briefly summarize, your entire statement will be made part of the record.

Mr. CARTY. Thank you. We also would like to see an amendment to section 5(M)(1)(b) of the act so that due process safeguards are included in the civil penalties section. Some notice requirements and some participation requirements. The rationale for this is outlined in our statement.

Also, we would like to see a cap put on the civil penalties—correction, the liability of organizations for violations of the FTC Act. At the present time, a company can face multimillion-dollar liability for a deceptive act or practice and we would like to see some cap put on that liability.

We also would like to see continuations of a number of sections of the Improvements Act of 1980 which would include a cap on intervenor funding, a moratorium on regulating commercial advertising and authority for the legislative veto.

That concludes my statement, thank you.

[The statement follows:]

STATEMENT OF JAMES P. CARTY, ON BEHALF OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. Chairman, for the record, I am James P. Carty, Vice President and Manager of the Government Regulation and Competition Department for the National Association of Manufacturers "NAM". I appear before you today accompanied by Mr. Howard A. Vine, Director of the Corporate Governance and and Competition Committee of the NAM.

The NAM welcomes this opportunity to testify before your Subcommittee to present our views on the reauthorization of the Federal Trade Commission "FTC". The NAM is a voluntary business organization of approximately 12,000 members and has affiliations, through its Associations Department and the National Industrial Council with an additional 158,000 businesses. In total, NAM members account for nearly 80 percent of the nation's industrial output and 85 percent of the nation's industrial workforce.

NAM members are highly sensitive to the impact of FTC actions upon their businesses, both from the perspective of the Commission's antitrust or "unfair methods" jurisdiction and from the Commission's consumer prohibitions on "unfair or deceptive acts or practices." NAM members view the reauthorization process as a significant opportunity to reexamine areas in FTC practice needing refinement.

The FTC is an agency of Congress. As the FTC Improvements Act of 1980 illustrated, the reauthorization process permits Congress, the public, and the federal agency the opportunity to reconsider both the direction of the underlying mandate and the means by which such responsibilities are carried out. As was evident with the FTC reauthorization process conducted in 1979/80, and bearing in mind that all Commission powers emanate from Congress, Congress proceeded with the view that limitations on the agency's exercise of federal investigatory and enforcement authority were needed. While the underlying policies of the agency remained in tact, Congress, based upon evidence brought to light during reauthorization hearings, reached a consensus regarding the need for limitations upon the discretionary enforcement power of the agency.

The fact that the FTC remains on a short-swing reauthorization process of a 2-year cycle allows constituents of the agency, including the NAM, the opportunity to bring before Congress relevant information relating to the success or failure of the agency in handling its mission. As has been seen in recent times, the reauthorization process, particularly with respect to the FTC, has taken on added importance. The basis for this heightened sensitivity to FTC authorization results from an acknowledged need for additional clarity of the Commission's discretionary authority and compliance requirements, increased awareness of the FTC's prosecutorial weapons and their potential for abuses. We need not dwell upon actions initiated during the 1970s which document the potential for abuse of FTC authority, or the great magnitude of resulting costs incurred in attempting to mitigate and prevent such intervention. For purposes of this statement, we need only cite the shared monopoly case against the cereal industry which the Commission pursued with all vigor—based upon no more authority than the broad discretion bestowed upon the agency under the vague concept of unfairness and without any corresponding basis in fact or necessity. Under its consumer jurisdiction we need only cite the lengthy, expensive, and futile attempt to regulate and prohibit advertising directed at children, once again on the theoretical basis of unfairness. The FTC is more than a dozen proposed rules continues to attempt to regulate many of the sectors of our economy, for example so-called "product quality" issues, that have never before been regulated and indeed have been repeatedly rejected by Congress as fit areas for FTC intervention.

The ramifications of an arm of the federal government pursuing a course of action premised upon theory, speculation and misguided instinct are serious. Cost estimates in the aborted effort to challenge children's advertising place the incurred costs in government man-hours and exorbitant legal fees by parties in that single case at approximately $35 million. In that case, Congress imposed a moratorium on FTC rulemaking in the children's advertising area. There is uniform acceptance that actions of the federal government must strictly conform to the policy guidance enunciated both in statutory language and common sense. In both the "Kid-Vid" and "shared monopoly" cases, statutory amibiguity was such as to permit FTC overreaching.

In "Kid-Vid," the matter was allowed to progress to a point which necessitated a congressional response. The "shared monopoly" case commanded in excess of 10 years of time, talent and resources to establish that the action should never have been brought. These cases illustrate the need for Congress to rechannel the allocation of Federal Trade Commission resources to areas legitimately the subject of federal action.

The NAM views federal intervention, through the FTC or other agency action, as a course which should be pursued with caution. The vast power and resources of the federal government should be reserved for those cases where statutory policy guidance is explicit, substantial injury is likely to occur and could not be reasonably avoided, and the costs of the injury have a net effect which outweigh the overriding benefits to consumers or competition. The actions of the federal government must be restrained and the exercise of discretion should weigh heavily on the side of caution absent any legally supportable basis of need. NAM specifically urges that Congress, during this reauthorization process, focus upon the elements which form the basis for prosecutorial and rulemaking discretion of the FTC. Such a focus, we believe, will lead Congress to the recognition that past experience with the lack of statutory checks on the zealousness of the Commission staff evidences a need for clear congressional direction to the FTC. Further, the NAM suggests that Congress employ this authorization process to channel the resources of the Commission and to enunciate with clarity the bases both for federal intervention and the imposition of penalties which will be consistent with policies that seek to accomplish deterrence, punishment and compensation. Each of these points is discussed below, in addition to the NAM's position on those provisions contained within the FTC Improvements Act of 1980 which are due to expire on September 30, 1982.

UNFAIR METHODS OF COMPETITION

The NAM, so as not to detract from the need for Congress to focus on FTC jurisdiction relating to "unfair or deceptive acts or practices". has deferred comment on that portion of the FTC Act dealing with antitrust matters during these reauthorization hearings. This, by no means, should be construed as NAM acquiescence to the present formulation, interpretation and application of that jurisdiction. Rather, the NAM considers the "unfair methods" jurisdiction to be, like the "unfair or deceptive acts or practices" jurisdiction, also subject to added clarification and codification by Congress. By separating out this issue during these authorization hearings, the NAM urges that Congress soon return to consider the enforcement ramifications of the present application of "unfair methods". Such a focus on "unfair methods" jurisdiction should closely follow Congress' resolution of the definitional and prosecutorial difficulties inherent in the application of "unfair or deceptive acts or practices".

FTC PROSECUTORIAL DISCRETION/"UNFAIR OR DECEPTIVE ACTS OR PRACTICES"

The issue of greatest concern to the membership of the NAM, at this time, stems from the ability of the Commission, under Section 5(a)(1), to challenge conduct on the basis of a prohibition on "unfair or deceptive acts or practices." That provision was created by Congress to bestow upon the FTC power to prevent conduct which bears no tangential relationship to competition; as had been required prior to enactment of this amendment. While "unfair methods" jurisdiction was central to the creation of the Commission, and was intended to be responsive to a congressional perception that the courts were emasculating the express prohibitions found in the Sherman antitrust statute, it was found that court decisions were limiting FTC intervention to cases involving some form of anticompetitive behavior. In 1938, Congress, again employing the term "unfair," extended Section 5 ("methods" jurisdiction) to include the express prohibitions on "unfair or deceptive acts or practices."

The NAM membership has struggled to define the meaning of the term unfair. As constituents of the FTC subject to potential prosecutions and rulemakings, NAM members have sought to carefully interpret the legislative history and court decisions concerning the meaning of unfairness.

The legislative history accompanying Congress' enactment of unfairness provides little guidance for purposes of aiding compliance. The legislative history merely affirms that the term "unfair" is an ambiguous standard subject to subjective interpretation.

The NAM is certain that, without congressional input on the elements that form the basis for Commission actions, neither reliance nor clarity will be reflected in FTC actions. The fact that the leadership of the Commission is subject to change provides little assurance that earlier FTC statements of Commission interpretation will govern. Similarly, as the issue of unfairness now stands, the subjective determinations as to what form of conduct constitutes "unfairness" will remain vested in the whims and prejudices of the Commission staff and members.

The only clarity that can be achieved and which will provide constituents of the Commission with both protection from overreaching federal intrusion and some degree of certainty is to establish a series of criteria, each of which must be met prior to the FTC challenging any form of conduct premised upon consumer unfairness. By adopting this position, the NAM is urging Congress to reconsider the circumstances in which Commission action is desirable and productive to the consumer.

The NAM is confident that the past problems that have befallen the FTC and its constituents—needless prosecutions, improper allocations of resources, and vast expenditures of dollars-can be avoided through codification of prosecutorial and rulemaking standards.

NAM's recommendation for threshold criterion, which would be required to be met by the FTC prior to taking action, are founded in logic and fairness. The tests which the FTC endorsed and which we support are embodied in the March 5 Commission letter to the Senate Commerce Committee. It would require the Federal Trade Commission and its staff to demonstrate the bases which suggests a need for federal involvement.

NAM's recommendation for a prosecutorial test is composed of three elements: (1) foreseeable substantial consumer injury; (2) inability of consumers to reasonably avoid such injury; and (3) the conduct in question should have net detrimental effects upon either consumers or competition generally. In other words, the conduct in question is not outweighed by countervailing benefits or costs. Each of these elements, in our opinion, should be considered and viewed as essential determinations prior to commitment of the resources of the FTC on a particular cases. Actions should be premised solely on the establishment of each criterion. Failure to substantiate a basis of action because one element may be lacking would serve to prevent any FTC involvement.

SUBSTANTIAL CONSUMER INJURY

The first element should be the most basic consideration of any federal prosecution—the need to prevent harm. Per our proposal injury must also be substantial. This test would require the Commission to take a questionable consumer practice one step beyond the intuitive finding that conduct may potentially or even actually result in consumer injury. The Commission would be required to show, on the record, that the actual injury at issue could reasonably have been foreseen. Thus, the Commission must clearly prove that enough information exists by which the Commission can draw the conclusion that absent federal intervention injury is not only likely to occur, but is foreseeable under the circumstances.

The injury must be of such substantial nature as to plainly justify federal intervention. As the Commission stated in its December 17, 1980, letter to Congress concerning unfairness:

"Emotional impact and other more subjective types of harm * * * will not ordinarily make a practice unfair. Thus, for example, the Commission will not seek to ban an advertisement merely because it offends the tastes or social beliefs of some viewers." (p. 6)

We fully agree with this initial formulation of the meaning of substantial consumer injury. However, we view this formulation as initial because it has been cast in a negative manner as to what shall not be deemed substantial. We urge Congress to follow the Commission's most recent elaboration (March 5, 1982) on the meaning of substantial consumer injury and we suggest that this principle be codified so as to provide more certainty. In the March 5, 1982, letter, the Commission states:

"As a general proposition, substantial injury involves economic or monetary harm and does not cover subjective examples of harm such as emotional distress of offenses to taste or social belief." (March 5 Commission letter at page 8.)

AVOIDABILITY OF CONSUMER INJURY

The NAM also supports the Commission with regard to the test for actionable consumer injury. In its March 5, 1982, letter, the Commission formulated this test as follows:

"* * * an unfair act or practice must be one which consumers could not reasonably have avoided. The commission should not be involved in rectifying the unfortunate choice of a particular consumer decision. It should confine its activities to curb behavior that takes unfair advantage of consumers' inadequate knowledge in reaching a decision or inability to protect themselves from such behavior." (letter at p. 8).

NAM recommends that this principle be codified. Each branch of the FTC's three-pronged test for consumer injury is of significance from a technical and legal point of view. This requirement—that the Commission act only where consumers have no reasonable means of protecting themselves—is critically important. Indeed, it is the key to ensuring that FTC actions are meaningful contributions to the functioning of a free marketplace.

The FTC position supported by the NAM is no retreat to the old days of "let the buyer beware." Under the "reasonably avoidable" standard, the Act (Section 5) would continue to reach abusive conduct which distorts or frustrates free consumer choices. Examples would include the selling of phony cures to seriously ill cancer patients.[1] or refusing to reassemble appliances supposedly dismantled for inspection until a contract is signed.[2] Both of these examples, drawn from established FTC precedents, illustrate consumer harm which would continue to be actionable.

At the same time, the FTC's practical approach clearly confirms that the Commission has no place as a "national nanny" or a utopian social and economic engineering agency with a mandate to tell Americans what is good for them. For example, where adequate maintenance, use and care information for a product is available, consumers who come to grief because they choose to ignore this information should not be treated as wards of the federal government. NAM policy language is explicit in supporting and encouraging disclosure of information to consumers. After all, if a seller's product is unsuitable or the seller's conduct is in fact unreasonable, consumers in the marketplace will penalize it far more effectively than the Commission.

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[1] See, e.g., *Travel King Inc.*, 86 F.T.C. 715, 774 (1975).

[2] *Holland Furnance Company* v. *FTC*, 295 F.2d 302 (7th Cir. 1961); cf. *Arthur Murray Studio Inc.* v. *FTC*, 458 F.2d 622 (5th Cir. 1972).

At the core of our social and economic system is our faith in free and informed individual decision making. In the political arena, our society tolerates no interference with the individual's free choice in the voting booth. In the economic sphere also, we should tread cautiously before stripping the individual of his rights and responsibilities as a consumer.

COUNTERVAILING BENEFITS

The NAM considers the likelihood of countervailing benefits of great significance in reaching a final conclusion that an FTC prosecution or rulemaking initiative is warranted. The determination of countervailing benefits will force a matter in question to be fully balanced between the potentially harmful act or practice and the net practical benefit to consumers or competition. This balancing of interests would require the Commission to quantitatively and qualitatively reduce its perception of a potential injury by the factors of economic and social costs and benefits that a practice may entail. In reaching this determination of "net" effects, the Commission should account for the costs of a prospective remedy, costs to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and capital formation and other similar considerations.

The NAM views the Commission letter of March 5, 1982, as constructive in this respect and urges Congress to codify the principles and intent of that letter. The Commission's letter states a position wholly consistent with that of the NAM with regard to countervailing benefits:

"* * * the injury should not be outweighed by consumer or competitive benefits resulting from the challenged practice. Clearly, most business practices involve an economic and social mixture of costs and benefits; hence, unless a particular practice has the *net* effect of being injurious, the Commission should refrain from finding it unfair. In reaching its decision, the Commission should take into account costs related to a propsective remedy, including but not limited to direct costs to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and capital formation and like matters." (letter at p. 8, emphasis supplied)

SUMMARY OF THREE ELEMENT TEST

The NAM urges Congress to enact and codify a three element requirement which, upon being met, would substantiate a basis for FTC actions premised upon "unfair or deceptive acts or practices" jurisdiction. As evidenced by the Commission in its letter to Congress dated March 5, 1982, the three criteria—substantial consumer injury, reasonable avoidability and lack of countervailing benefits—properly reflect a reasoned approach to balancing the federal interests in prosecution with the costs and benefits which may result from a questioned practice. This test further illustrates and reflects the sensitivity of Congress, the FTC and its constituents to the need to confine government intervention to acts and practices that require the powers and resources of the federal bureaucracy.

In principle, each element of the three-pronged test is supported by the present Commission. The only dissent that apparently exists relates to the recommended approach of codifying and setting into statute these proecutorial and rulemaking standards. The distinct differences between the Commission interpretation of consumer unfairness issued in 1980, and the recent elaboration of March 5, 1982, evidences the fact that Commission composition can influence the level of discretion under an unfairness interpretation. So that members of the NAM, the business community and others may conduct their businesses and relationships with the federal goverment in a rational and consistent manner, we urge Congress to codify these terms and elements. While there is some truth to the dissenting statement of Commissioner Pertschuk, the potential for long-term future clarity will outweigh the costs of insecurity and ambiguity.

We commend the Commission for their most recent statement and wish to express both our satisfaction in their commitment to clarity and consistency in the use of the unfairness doctrine.

SECTION 5(M)(1)(B)—REMEDIES AND VIOLATIONS

The NAM suggests that Congress reconsider the present construction and underlying basis of Section 5(m)(1)(B), the civil penalty section. While valid arguments exist which would support repeal of this section, the NAM urges Congress to do no less than amend the Commission's 5(m)(1)(B) authority.

Under Section 5(m)(1)(B), the Commission may seek to impose civil penalties of up to $10,000 against companies who allegedly violate final cease and desist orders entered in proceedings against other firms. NAM's concerns relates to the inherent lack, within the substantive and procedural terms of Section 5(m)(1)(B), of due process accorded parties subject to the provision. Section 5(m)(1)(B) permits the FTC to impose penalties and requirements upon companies who were not parties to, nor provided notice and opportunity to be heard in, original cease and desist proceedings.

NAM urges that should Section 5(m)(1)(B) authority continue, Congress must ensure that all elements of "due process," including notice to be heard and opportunity to participate, be required as a statutory procedural requirement for the implementation of Section 5(m)(1)(B) penalties.

Another serious problem revolves around the different possible interpretations of what constitutes a "violation" of § 5, and how large the money penalties may be (which depends on how one counts "violations").

At present, § 5(l) of the Federal Trade Commission Act imposes a "civil penalty of not more than $10,000 for each violation" of an order of the Commission; it also provides that "[e]ach separate violation of such an order shall be a separate offense." But the statute gives no guidelines as to what constitutes a "violation."

Section 5(m) provides a similar $10,000 civil penalty for "each violation" of a Commission rule, but also fails to define a "violation."

In the absence of guidelines as to what constitutes a "violation," however, a businessman cannot predict his possible exposure for civil penalties. Will it be $10,000 for a single violation, or will it be $10,000 for each of serveral violations? If there is even a remote chance for the latter, the manager may forego legitimate and constitutionally protected activity. As important, if the Commission should later seek civil penalties, the business manager's legal adviser will be hard pressed to give any accurate assessment of the potential exposure. The decision to defend an action, with a reasonable defense, will be based solely on the potential exposure rather than on the merits of the case. Consequently, the civil penalty process is likely to be protracted, with no clear benefits for the consumer public or society in general.

NAM's concerns are not unrealistic. Internal guidelines, which recently became public, have been developed at the FTC.[3] Those guidelines refer to a 1982 civil penalty action over two misleading ads that appeared in 302 comic books. Nine separate publishers printed and distributed more than 25 million copies. The government alledged, and the court found, only nine violations—one for each of the publishers. But the court's opinion stated that "in reality each comic book published and mailed which reaches the hands of a recipient is a violation of the Order."[4] As a result of that dictum, the Commission staff now believes that, for the same conduct that led to a civil penalty for nine violations in 1962, it now could sue for up to 25 million violations.[5]

Recently, the Commission has begun to exercise this "discretion." For example, in a penalty action in California, respondent had filled some 252 orders for 21 different printed forms allegedly in violation of a Commission order, selling in all more than 305,000 of the printed forms. The government contended that each of the forms sold to creditors and debt collection agencies constituted a separate violation. In 1980, the court agreed, and found more than 305,000 violations.[6] And just last year in Philadelphia, the United States Court of Appeals for the Third Circuit affirmed a civil penalty judgment holding that each of some 16 million advertisements distributed in six bulk mailings constituted a separate violation, and that each of the so-called violations was subject to a maximum penalty of $10,000.[7]

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[3] See "FTC Oversight: The JS&A Case," Hearing Before the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce, H.R. (97 Cong., 1st Sess.) Serial No. 97–38, September 18, 1981, p. 232 (hereinafter "JS&A Oversight"). It is unclear whether these "guidelines have the imprimatur of the full Commission, or merely reflect the legal research of one FTC staff member (see id., p. 231).

[4] *United States* v. *Wilson Chemical Company, Inc.* (W.D.Pa. 1962) 1962 CCH Trade Cases ¶ 70,478, at p. 76,957, affirmed per curiam (3 Cir. 1963) 319 F.2d 133.

[5] The guidelines for the Assessment of Civil Penalties or other Equitable Relief state: " * * * the Commission can frame its Complaint so that such disseminations are broken down, for example, by states, by dates mailed, by different zones or by different issues in which the advertisement appeared. Thus, depending upon how the violation is charged, the Complaint may allege a million violations (the number disseminated), 50 violations (the states in which the comic books were disseminated), 15 violations (the dates on which they were mailed), five violations (the zones), or one violation (the single magazine in which the ad appeared)" (JS&A Oversight, p., 251) (footnote ommitted.)

[6] *United States* v. *Floersheim* (C.D.Cal. 1980) CCH Trade Cases ¶63,368, at p. 75,872 affirmed (9 Cir. 1981) 659 F. 2d 1090.

Traditionally, there are three legitimate functions for a civil penalty provision: (1) compensation (when injury occurs); (2) deterrence; and (3) punishment of wrongdoers. Because penalties under the FTC Act are paid to the general treasury, the importance of the compensation function to § 5 is less than clear. In any event, the purposes for the penalty provision can be served adequately if the civil penalty sections are amended to ensure that the interpretation of the statute and the penalties imposed are rational and predictable.

We therefore propose two amendments: (1) to clarify that a "violation" should be defined so that the penalty bears a relation to the actions of the alleged wrongdoer and to the number of decisions the business manager makes; and (2) to place a cap on the amount of the civil penalty that may be imposed for offenses that arise from a common plan or a single business course of action.

We believe the amendments we propose strike a fair and reasonable balance of legitimate government goals, while providing clear and predictable standards to guide business managers in their behavior. If the FTC Act is amended as we propose, substantial penalties will be available to deter multiple violations. The government will also be free to seek even stiffer penalties from those who continue to violate Commission orders or rules, and to obtain contempt citations with commensurate fines and other sanctions against scofflaws. But legitimate publishers, advertisers and broadcasters who make a single decision (later determined to be erroneous) and disseminate material (later determined to violate an order or rule) will no longer be threatened with unreasonable multiplication of violations and devastating penalties or even possible bankruptcy.

ISSUES SUBJECT TO EXPIRATION UNDER THE FTC IMPROVEMENTS ACT OF 1980

Section 10 (a).—Intervenor funding: NAM has long opposed the funding, through taxpayer's dollars, of witnesses and public participants in agency rulemaking proceedings. Our premise throughout has been that the funding of intervenors extends beyond the policy justification of encouraging a broader range of views to agency proceedings, to having the general revenues supporting the arguments and philosophy of a small segment of the public. In this regard, NAM was active in opposing Section 18(h) (Intervenor Funding) of the FTC Act, and correspondingly was greatly supportive of the amendments in the 1980 FTC Impovements Act, which placed a cap on the level of compensation which may be paid to rulemaking participants. Although the Commission, at this time, has no funds with which to carry out any form of intervenor funding program, the cap on disbursements under that program are subject to expire, and the NAM wishes to again express its disapproval of any form of intervenor funding program and urges at a minimum continuation of the current cap.

Section 11(b).—Commercial Advertising: The NAM supported the moratorium which was placed upon Commission activities relating to rulemaking and regulation on the basis of "unfairness" of commercial advertising. That moratorium is scheduled to expire on September 30, 1982. As pointed out earlier in our statement, the NAM urges Congress to provide for added clarity and control over "unfair or deceptive acts or practices" jurisdiction. In this regard, NAM continues to support limiting the ability of the Commission to pursue bans directed at both commercial speech and commercial advertising based upon theories and interpretations of "unfairness." This position, we believe, is consistent with the approach we recommend be taken on prosecutorial and rulemaking discretion and is intended to supplement imposition of an "element" test.

Section 21.—Legislative Veto: The entire legislative veto mechanism (including the appeals procedure) is slated to terminate after September 30, 1982. NAM has long supported imposition of a legislative veto mechanism for reasons of fairness and as a means to provide a check and balance upon the regulatory system. NAM will continue to press for legislative veto throughout the regulatory process and, in this regard, urges Congress to make permanent the temporary legislative veto.

This concludes our prepared statement, and we will be happy to respond to any questions.

Senator **Kasten**. Thank you, Mr. Carty. Our next witness is Mr. Jared Blum, Small Business Legislative Council.

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[7] *United States* v. *Reader's Digest Association, Inc.* (3 Cir. 1981) 662 F.2d 955, certiorari denied (January 18, 1982)——U.S.——

Mr. **Blum**. Thank you, Senator. I am here today on behalf of the Small Business Legislative Council. I serve as their Vice Chairman and also as Chairman of their Antitrust Committee. At the outset, I want to comment on Senator Kasten's remarks and Senator Packwood's remarks with respect to the intent of the committee not to deal with the antitrust authority of the Commission and the small business community applauds that decision.

We think that the antitrust authority of the Commission should be left intact. We would like to make it even stronger, but we would be satisfied with it being left intact for now.

Mr. Chairman, we applaud the efforts of this Congress and this administration to restore fiscal responsibility to all aspects of Federal spending. This means that some agency budgets must and should be cut. It does not and should not rule out, however, a close look at what funds are being cut and by how much. Congress must ask what legislative or executive functions and activities are being curtailed or eliminated and then determine if the specific proposals are prudent and wise.

The continued existence of a viable and growing small business segment of our economy is not at all based on sentiment, a longing for the good old days, for the familiar cornerstore or one-man or one man and one wife shop. Thus, Congress and the executive branch have, over the decades, developed policies and programs which foster and encourage small business. These policies are based on sound and most practical considerations.

Chief among these has been the growing recognition that it is the small business, not big, that lead in the creation of new jobs. It is small business, not big, that leads to innovation. Also, it is the small business unit upon which we must rely to provide the essential element of competition so as to protect all of us against the abuses of monopoly power, the deliberate limiting or production to sustain ever higher prices, the divisions of markets and customers, and even price fixing.

The Federal Trade Commission was organized in 1914 to supplement and further our national policy of encouraging competition in the Nation's marketplace, and thus, to encourage small business. This policy is the antithesis of regulation by Government. Rather, the founding of the Federal Trade Commission was an act of faith in the virtues of our free enterprise system. The primary and vital mission of the FTC was and has been antitrust, to keep the channels of commerce open and free from the competition-destroying and initiative-deadening, monopolistic practices that would otherwise soon emerge.

In furtherance of its antitrust mission, the FTC has proceeded in two special and unique ways. One is its ability to proceed against antitrust violations in their incipiency; the second is the enforcement of the Robinson-Patman Act and I know this is something that we are all familiar with and I will just dwell on it for just a moment.

Robinson-Patman Act, we are aware, has come under critics' charges that it results in higher prices to the consumer. But we have not any—I stress this—any factual data to support the charge, nor do we think that the charge can withstand any careful scrutiny. Essentially, the act requires that the same prices be made available to all with adjustments based on cost-justified volume and other legitimate factors. The Small Business Legislative Council is greatly concerned that budget constraints will encourage Commission leadership to succumb to the temptation to let Robinson-Patman enforcement die.

While the Commission has not always exercised good judgment in the area of consumer protection, as a matter of history it has been the FTC that has been sensitive to the needs of small business. It has been sympathetic to the problems visited upon the small business when large competitors seek to obtain an unfair advantage over smaller rivals.

With the above as background, we wish to address the specific question now before this committee. We indicated above our grave concern about using the budget process to emasculate the Commission's historic mission. The Commission's budget should be maintained at levels consistent with vigorous antitrust efforts. We are not in a position to specify exactly what funding level is appropriate; however, it seems clear to us that a continued diminution in the agency's appropriations can only result in the eventual loss of capability to fulfill basic objectives that all observers, including the three on this panel, can agree upon. A viable independent regulatory agency, one that is unyielding to political pressures, is essential.

We cannot avoid commenting, therefore, on the levels of funding now proposed by the Commission and the Office of Management and Budget. To allow a 22 percent gross reduction in the Commission's budget over the next 3 years would seem to us necessarily to result in substantially lower Commission effectiveness.

If you will grant me 2 more minutes, Senator, I will get into the unfairness and the professional regulation issue. Legislation pending before your committee which would exempt State-regulated professions from FTC jurisdiction is of concern to the small business community. This could provide most unfortuate results for small business that utilize all sorts of professional services. Before a broad-range proposal like this is adopted, we would urge further hearings, even though you have them already, on the issue as to its impact on small business and as to whether or not States attorneys general feel they could adequately police restraints of trade by State professional groups.

Other proposals which may have more meritorious intent such as clarifying the meaning of unfairness as it relates to the Commission's consumer protection function may be premature. Though predictability in law enforcement is a desirable goal, the Commission in its December 17, 1980, policy statement to this committee, recognized the strictures that existing law imposes on its consumer protection mandate.

In our judgment, a careful and precise analysis must be made of any proposed changes in section 5, even if not directly connected to the Commission's antitrust mission. We respectfully suggest that this is not the time to accomplish such analysis.

[The statement follows:]

STATEMENT OF JARED O. BLUM ON BEHALF OF THE SMALL BUSINESS LEGISLATIVE COUNCIL

Mr. Chairman and members of the committee, this statement is submitted on behalf of the Small Business Legislative Council (SBLC), an organizaton of 70 national business and trade associations. In turn, our members represent about 4.5 million small business units covering almost the full range of SIC classifications.

My name is Jared Blum. I am the Vice Chairman of SBLC and the Chairman of its Antitrust Committee. I also am Vice President and General Counsel of the Direct Selling Association. I am accompanied here today by Thomas A. Mauro, antitrust counsel to the SBLC and a member of its Antitrust Committee.

At the outset, Mr. Chairman, we applaud the efforts of this Congress and this Administration to restore fiscal responsibility to all aspects of federal spending. This means that some agency budgets should be cut. It does not and should not rule out, however, a close look at what funds are being cut and by how much. Congress must ask what legislative or executive functions and activities are being curtailed or eliminated, and then determine if the specific proposals are purdent and wise.

The Small Business Legislative Council requests that most careful consideration be given by Congress as to any proposals to utilize the budget and budget-cutting processes to bring about substantial changes in the historic missions of the Federal Trade Commission. Before discussing the details and reasons for small business opposition to attempts to perform radical surgery on the FTC via the budget process, it is appropriate that the foundations for our grave concern about this matter be started.

The continued existence of a viable and growing small business segment of our economy is not at all based on sentiment, a longing for the good old days of the familiar corner store or one man or man and wife enterprise. Thus, Congress and the Executive branch have, over the decades, developed policies and programs which foster and encourage small business. These policies are based on sound and most practical considerations. Chief among these has been the growing recognition that it is the smalls, not the bigs, that lead in the creation of new jobs. It is the smalls, not the bigs, that lead in innovations. Also, it is the small business unit upon which we must rely to provide the essential element of competition so as to protect all of us against the abuses of monopoly power, the deliberate limiting of production to sustain ever higher prices, the divisions of markets and customers, and even price fixing. Our economy today abounds with examples of the influence of new and innovative and sometimes revolutionary products which are the result of small business enterprise.

The Federal Trade Commission was organized in 1914 to supplement and further our national policy of encouraging competition in the nation's marketplace and thus to encourage small business. This policy is the antithesis of regulation by government. Rather, the founding of the Federal Trade Commission was an act of faith in the virtues of our free enterprise, competitive systems. The primary and vital mission of the FTC was and has been antitrust, to keep the channels of commerce open and free from the competition-destroying and initiative-deadening monopolistic practices that would otherwise soon emerge.

In furtherance of its antitrust mission, the FTC has proceeded in two special and quite unique ways. First, under Section 5 of the Federal Trade Commission Act, the Commission can reach those acts and practices that tend to be destructive of competition and tend toward monopoly, whether engaged in by one firm or by several. The Department of Justice cannot do this, for they must prove the existence of a conspiracy or, alternatively, something close to actual monopoly under the constraints of Section 2 of the Sherman Act. Thus, the Department of Justice does not have the legal means to challenge individual conduct that is undesirable as being anti-competitive, unless they are dealing with a monopoly situation. These are not the usual kind of cases.

Briefly stated, then, it is the FTC and only the FTC that can control most individual conduct that is undesirable as being anti-competitive and inconsistent with accepted competitive business conduct.

The second unique area of FTC antitrust enforcement is that the FTC—and only the FTC—enforces the Robinson-Patman Act. To preserve competitive opportunity for small business, Robinson-Patman was enacted to stop in their incipiency anti-competitive practices which have plagued this country. Essentially, the Robinson-Patman Act is intended to ensure that small businesses can buy on the same terms and conditions as can large busineses. It forbids price discrimination between purchasers of goods of like quality in interstate commerce, where the effect of such discrimination "may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

We are aware of the critics, charge that Robinson-Patman results in higher prices to the consumer. We are not aware of any factual data to support the charge, nor do we think the charge can withstand careful scrutiny. Essentially, the Act requires that the same prices be made available to all with adjustments based on cost-justified volume and other legitimate factors. If a manufacturer, for example, sells at his lowest reasonable price to all, then all customers will benefit through the ensuring price competition of healthy, vigorous dealers.

The Robinson-Patman Act is no more or less a reflection of national policy that such should be preserved. It is a fundamental antitrust statute that demands the total support of government. The Small Business Legislative Council is gravely concerned that budget restraints will encourage the Commission leadership to succumb to the temptation to let Robinson-Patman enforcement die.

We believe any proposal to significantly limit the Commission's mission is in reality a proposal jeopardizing a broad spectrum of present antitrust law. A wave of anti-regulation emotion should not be converted into anti-antirust emotion.

While the Commission has not always exercised good judgment in the area of consumer protection, as a matter of history, it has been the FTC that has been sensitive to the needs of small business, that has been sympathetic to the problems visited upon a small business when its larger competitors seek to obtain an unfair advantage and oppress their smaller rivals. In such instances the FTC has been willing to employ its legal mechanisms, its jurisdiction, to help keep the competitive contest a fair contest. History teaches that, left to its own devices, with no enforcement of the rules of fair play, competitive processes do not continue to exist. They are soon destroyed, and monopolies emerge. This, in turn, inevitably leads to an outcry for regulation by government, which none of us wants.

With the above as a background, we wish to address the specific question now before this Committee. We indicated above our grave concern about using the budget process to emasculate the Commission's historic mission. The Commission's budget should be maintained at levels consistent with vigorous antitrust efforts. We are not in a position to specify what funding level is appropriate. However, it seems clear to us that continued diminution in the agency's appropriations can only result in the eventual loss of capability to fulfill basic objectives—both antitrust and consumer protection—that all observers can agree upon. A viable independent regulatory agency, one that is unyielding to political pressures, is essential. You have that in the FTC.

We cannot avoid commenting, therefore, on the levels of funding now proposed by the Commission and the Office of Management and Budget. To allow a 22 percent gross reduction (before the effects of inflation are considered) in the Commission's budget over the next three years would seem to us necessarily to result in substantially lower Commission effectiveness. We ask that the proponents of this proposal accept the responsibility before this Committee of demonstrating why the proposed reduction will not result in an actual reduction of the Commission's mission.

Related to our concern over an actual diminution of the Commission's enforcement mission is the question of the closing of FTC Regional Offices. The small business community certainly opposes the wholesale closing of such offices, but agrees with the present Commission plan to continue at least 6 regional offices in light of budgetary constraints. Enforcement of the rules of competition in the market areas where they are taking place is of vital concern to small business. Small business needs an antitrust presence—a cop on the beat.

But more than just a presence is needed. The injured small business proprietor may and does call on the Regional Office to give voice to his competitive problems. A trip to Washington, D.C. is, for the most part, out of the question. Available time and money simply do not permit a trip of this nature to be made by most small business firms. Moreover, to attempt to develop the pertinent facts by correspondence with a distant office would be a frustrating and inadequate exercise.

We do not wish to see Commission enforcement in the field written off. If cut backs in Regional Offices are inevitable, and it seems that they are, we urge this Committee and the Federal Trade Commission to see to it that a Regional Office structure that is evenly distributed geographically and which is designed to maintain strong Commission presence is preserved.

Since the issue before this Committee is reauthorization, we have focused this statement on the need for the agency and adequate funding for its activities. However, we also wish to express concern over legislative proposals that are not before this Committee today but upon which its members may have to vote in the future. It is somewhat distressing for the small business community to continually have to "defend" the FTC against proposals to reduce to restrict its jurisdiction made over the past several years. The Commission has made errors, no one would deny, and the 1980 FTC Act amendments have gone a long way to curb some abuses like the children's advertising rule and unfair subpoena enforcement procedures, to name a few. But the ink is barely wet on the 1980 proposals, and a new set is being prepared, many of which the SBLC has significant problems with accepting.

For example, legislation is pending before your Committee which would exempt state regulated professions from FTC jurisdiction. This could prove most unfortunate for small businesses that utilize all sorts of professional services. Before a broadranging proposal like this is adopted, we would urge further hearings on the issue as to its impact on small business and an inquiry as to whether the state attorneys general feel they could adequately police restraints of trade by state professional groups. I doubt the answer would be affirmative.

Furthermore, while no one would question the authority of a state to regulate purely intrastate activities, it is entirely another matter to arbitrarily limit the Commission's legitimate federal jurisdiction over the activities of professional groups. It seems to us that it would be folly to deprive the Commission of the flexibility of addressing itself to significant regional issues concerning professional groups and thereby render such groups above the law that applies to the rest of us. We have seen antitrust concepts improve consumer welfare in the area of professional activities, securities regulation, real estate and legal services, to name but a few. There is no reason to think that such benefits will not continue under current enforcement plans.

Other proposals, which may have more meritorious intent, such as clarifying the meaning of "unfairness" as it relates to the Commission's consumer protection function, may be premature. Though predictability in law enforcement is a desirable goal, the Commission in its December 17, 1980 policy statement to this Committee recognized the strictures that existing law imposes on its consumer protection mandate. In addition, the judiciary has carried out its obligation to flesh out Congressional intent as it concerns the language "unfair . . . or deceptive acts of practices."[1] In our judgment, a careful and precise analysis must be made of any proposed changes in Section 5 even if not directly connected to the Commission's antitrust mission. We respectfully suggest that this is not the time to accomplish such an analysis. Is it necessary at this time to engrave in statute what the Commission has already adopted as its policy? Why not see how the FTC's "substantial consumer injury" approach works in practice before enactment of strict and complex statutory standards.

In conclusion, small business appreciates the opportunity the Committee has provided us to be heard on a matter of urgent and vital importance. We are pleased that you have allowed us to present our views and look to your continued interest in these questions.

[The following information was subsequently received for the record:]

Small Business Legislative Council,
Washington, D.C., April 7, 1982.

Hon. Robert Packwood,
U.S. Senate, Dirksen Senate Office Building,
Washington, DC 20510

Dear Senator Packwood: Many thanks for your letter of March 26, in which you request answers to three questions relating to my testimony before your committee regarding the FTC authorization bill. I am pleased to submit the following responses to your question:

1. Small businesses use the Federal Trade Commission regional offices in a number of different ways. First and foremost, existence of the regional office provides a deterrent effect for potential trade restraints. The "policeman on the beat" impact of some regional offices can't be overstated. In addition, small businesses usually do not have in-house counsel to advise owners of what may or may not be permissible acts by a competitor. Very often what is construed to be "against the

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[1] The Supreme Court at a very early stage in the Commission's development took the opportunity to remind everyone that the judiciary would carry out its constitutional role as concerning Section 5. In *Federal Trade Commission* v. *Gratz* (253 U.S. 4216 (1920)), the Court upheld the original Section 5 provision and reminded us that, although the words "unfair method of competition" are not defined and their exact meaning is in dispute, [i]t is for the courts, not the commission, ultimately to determine as matter of law what they include." 421 U.S. at 427.

law" by a small businessman is a permitted act and one phone call may assuage the ire of a small businessperson. The ability to call or visit an FTC office, explaining the facts of a given case, may disclose a pattern of conduct which prompts the regional office to make further inquiry to determine whether or not a violation has occurred.

With respect to your question regarding the minimal number of regional offices that should be maintained, it is the view of the Small Business Legislative Council that the proposed reduction from ten to six is acceptable and consistent with budgetary priorities of the commission. SBLC could not support the reduction of regional offices below that number at this time.

2. The SBLC opposes a statutory codification of the Federal Trade Commission's December 1980 policy statements on "unfairness" primarily on the issue of timing. It is the view of the small business community that many major changes have been wrought in the commission's authority over the last three or four years and that sufficient time should elapse to allow those statutory changes to be judged and, in addition to determine what impact the commission's codification has on the types of cases brought and the final determination in those cases. Specifically, to allow time for the Congress and the courts to judge whether or not the new standard is consistent with the commission's mission and continues to serve the public interest. The Small Business Legislative Council is not aware of any actions initiated under the new leadership at the commission which would indicate that the commission has departed from its policy statement so that a statutory codification would be necessary.

3. Though in the past the small business community has supported fair trade laws, with the repeal thereof in the mid-70's and the evolving rule or reason for other vertical restraints besides price restraints, SBLC would not support a weakening of the per se antitrust rule against resale price maintenance. While there is no SBLC official position in this area, it would be the view of the Antitrust Committee that a weakening of the per se rule would be inconsistent with the purposes of the antitrust laws and open the door to practices detrimental to the small business community.

4. In relation to your counsel's question concerning the provision of S. 1984 requiring reimbursement by the commission for compliance with its subpoenas, the Small Business Legislative Council has no offical position. However, though it would appear to be, at first blush, beneficial to the small business community to have compliance with the subpoena request reimbursed, the probable effect would be to force the commission to forego cases against large companies with massive costs for subpoena compliance and rather proceed against medium and smaller size companies to establish precedent because of the reduced cost of reimbursement for subpoena compliance there. Consequently, the Commerce Committee is urged to go very slowly in the area of subpoena compliance reimbursement so as to not indirectly force the commission, through budgetary considerations, to concentrate its enforcement areas in the small business community.

I hope these answers have been responsive to your questions and the Small Business Legislative Council appreciates your interest and deep concern for the wellbeing of the small business community in America.

Best personal regards.

Sincerely,

JARED O. BLUM,
Chairman, Antitrust Committee.

Senator **KASTEN**. Mr. Roland Brandel, Consumer Bankers Association. Mr. Brandel.

Mr. **BRANDEL**. Thank you, Senator Kasten. I am going to focus this morning on only one aspect of the FTC's current power and a need for congressional action. That is the need to repeal the FTC's inordinate power to make law to prohibit those practices the FTC deems to be unfair.

The FTC has very broad authority to prohibit conduct that it believes to be unfair. Under section 18 of the FTC Act, which grants the FTC explicit rulemaking power over unfair acts or practices, the agency can promulgate rules regulating virtually all aspects of our national economic life.

The FTC has legislative powers second only to that possessed by Congress itself, but without the checks on raw power that are applied to Congress. No bicameral check, no presidential veto and most importantly of all, no responsibility to an electorate, limit the FTC's power. Although this delegation of broad rulemaking authority may not be legally unconstitutional, it cuts across the grain of some of the most fundamental concepts upon which representative government is based.

The standards that guide the exercise of this power are at best open-ended and vague. The FTC does not function as do other regulatory agencies; it does not apply an expertise in a particular industry or economic activity to narrow, but complex matters. Rather, Congress has invited the FTC to make broad value judgments. The judgments of social policy exercised by the five appointed commissioners vested with this expansive rulemaking authority are, as a practical matter, subject only to limited judicial or congressional review, and then, only after costly rulemaking procedures have been completed.

Most importantly, these officials and their judgments are not subject to the ultimate repository of value judgments: The will of the public. When Congress delegated practically unlimited rulemaking power to the FTC, it abdicated its legislative function of democratically determining public policy.

The impact on the proper relationship between the Federal Government and the States is even more perniciously affected. What Congress did in giving the FTC this power was to wrest away from thousands of elected State officials, who are in close touch with the values of their communities, the power to make law and gave it to five appointed officials.

The FTC today can eradicate by administrative fiat the considered judgments of governmental officials and voters themselves, as reflected in constitutional, statutory, regulatory and judicial principles at the State level, if in its sole discretion it deems an act or practice to be unfair. This represents a fundamental restructuring of our Federal system. It is inconsistent with the commitment of the present administration to restore a proper balance of power between Washington and the States.

We welcome the FTC's recognition that external standards are necessary to limit their lawmaking function. We do not believe that the restrictions the FTC has recommended today are sufficient. The carte blanche rulemaking authority to regulate unfair acts and practices vested in the FTC by Congress under section 18 should be repealed.

Thank you.

[The statement follows:]

STATEMENT OF ROLAND E. BRANDEL ON BEHALF OF THE CONSUMER BANKERS ASSOCIATION

I am pleased to be invited to appear today on behalf of the Consumer Bankers Association. The Association is a national trade association whose more than 400 members hold more than 65 percent of the total consumer credit outstanding for all commercial banks in the United States. In dollar value, the outstanding consumer credit of CBA members amounts to in excess of $88 billion. I will focus quite specifically on one aspect of the present operations of the Federal Trade Commission: the need to repeal its inordinate power to make law to prohibit those practices it labels "unfair."

The Federal Trade Commission ("FTC") has very broad authority to prohibit conduct in or affecting commerce which it considers to be "unfair" or "depective." Under the overly broad language of Sections 5 and 18 of the Federal Trade Commission Act, especially the language granting the FTC explicit rulemaking powers over "unfair . . . acts or practices," the agency can promulgate rules regulating virtually all aspects of our national economic life. Thus the FTC has legislative power second only to that possessed by Congress itself, but without the checks on raw power that are applied to Congress. Although this delegation of broad rulemaking authority may not be unconstitutional, in the strict sense of the term, it cuts across the grain of some of the most fundamental concepts on which representative government is based.

The standards that putatively guide the exercise of this power are, at best, extremely open-ended, vague and imprecise. The judgments of social policy exercised by the five appointed commissioners vested with this expansive rulemaking authority are as a practical matter subject only to limited judicial or Congressional review, and then only after rulemaking has been completed. Nor are these officials and their judgments subject to the ultimate safeguard of the will of the public. When Congress delegated practically unlimited rulemaking power to the FTC, it abdicated its legislative function of democratically determining public policy.

The impact on the proper relationship between the federal government and the states is even more pernicious. The FTC may now eradicate by administrative fiat the considered judgments of governmental officials and the people themselves as reflected in constitutional, statutory, regulatory and judicial principles at the state level—if in its sole discretion it deems an act or practice unfair. This represents a fundamental restructuring of our federal system. It is inconsistent with the commitment of the present administration to restore a proper balance of power between Washington and the states.

While it may be desirable in certian circumstances to delegate to regulatory agencies like the FTC the task of making administrative rules having the force of law, that delegation should only be made within well defined policy parameters established by Congress in a specific statutory framework.

The carte blance rulemaking authority to regulate unfair acts and practices vested in the FTC by Congress under Section 18 should, therfore, be repealed.

I. THE GROWTH OF FTC POWER

The FTC was created in 1914 as an agency of quite limited powers, but has since become potentially one of the most powerful and active regulatory agencies in the federal government. The FTC's original mandate to prohibit "unfair" methods of competition was confined to controlling anticompetitive conduct. Its power to interfere in other aspects of the eocnomy was expressly limited in 1931 by the United States Supreme Court decision in *FTC* v. *Raladam Co.* (283 U.S. 647 (1931)), which held that Section 5 of the FTC Act did not prohibit conduct that was unfair to the consuming public unless that conduct also resulted in an injury to a competitor or the competitive process. In order to avoid the limitations imposed by *Raladam*, Congress in 1938 enacted the Wheeler-Lea Act, which added to the prohibitions of Section 5 of the FTC Act the words "unfair or deceptive acts or practices in commerce." This new mandate. aimed primarily at consumer harm, gave the FTC the power to police unfair trade practices without showing an anticompetitive impact.

The power of prohibiting trade practices, in the absence of deception or anticompetitive effect, solely on the ground of unfairness, was not claimed by the FTC as the explicit basis for trade regulation proceedings until the 1960's. This power, as a basis for cease and desist proceedings under Section 5 of the Act, was confirmed by the United States Supreme Court in 1972 in the landmark decision of *Federal Trade Commission* v. *Sperry & Hutchinson Co.* (405 U.S. 233 (1972)). In that case, the Court in effect gave the FTC almost unlimited authority to proceed in individual actions against trade practices on the basis of unfairness to consumers.

During the same period the FTC was for the first time attempting to use the sweeping "unfairness" concept to expand its powers beyond cease-and-desist proceedings to the promulgation of substantive rules that had the effect of statutory law. Whether the Act conferred on the FTC such a power to promulgate substantive rules was highly controversial.

In 1962 the FTC, relying on much-criticized interpretations of its authority, issued procedural rules for the promulgation of substantive trade regulation rules. The FTC, however, did not assert its rulemaking powers in an aggressive manner, and more than a decade passed before such an extraordinary power was clearly vested in the FTC.

In the early 1970's the issue was brought to a head in two forums, one judicial and one legislative. In *National Petroleum Refiners Association* v. *FTC* (482 F.2d 672 (D.C. Cir. 1973), cert. denied, 415 U.S. 951 (1974)), a case involving the validity of the octane rating trade regulation rule, the U.S. Court of Appeals for the District of Columbia, in reversing a lower court, held that the FTC Act did indeed confer the power to promulgate substantive rules. At the same time that the matter was pending before the Court of Appeals, legislation addressing the issue was moving through Congress, and in 1975, the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act (the "Magnuson-Moss Act") became law. Title II of that Act specifically grants to the FTC the power to prescribe substantive rules and also enhances the agency's enforcement powers. The result is that the FTC now possesses the authority to regulate conduct in all sectors of the economy, with the exception of a small number of exempt industries, subject only to the constraint that, in the judgment of the FTC, "unfair" or "deceptive" acts or practices are involved.

II. THE FTC'S UNLIMITED POWER TO PROMULGATE RULES PROHIBITING ACTS IT CONSIDERS "UNFAIR" REPRESENTS A BAD POLICY

A. The FTC's power is uniquely broad

Under the Magnuson-Moss Act the rules promulgated by the FTC may apply to any act or practice "in or affecting commerce," and the only statutory guide is that it be "unfair." The apparent power of the FTC with respect to business and consumer relationships is virtually as broad as that of the Congress itself. Indeed, the FTC may be the second most powerful "legislature" in the country. Under the Constitution's Supremacy Clause, the FTC has the power to declare any commercial act or practice to be "unfair" regardless of state law, and thereby to amend all state constitutional provisions and statutes and reverse all state judicial decisions that may be inconsistent with its declarations. But unlike Congress and other legislative bodies, its powers include other governmental functions. In its various capacities as investigator, prosecutor, judge, and lawmaker the FTC has used its powers to pursue everything from oil company divestitures to credit practices and breakfast-cereal advertising directed at children. FTC commissioners have claimed the power to be able to regulate everything from employment of illegal aliens to cheating on taxes.

Since it was originally introduced, there has been widespread concern among members of Congress that the standard articulated in the Magnuson-Moss Act governing FTC consumer protection rulemaking provided few real limits on agency power. Yet the limits Congress considered and ultimately enacted, both initially and in the FTC Improvements Act of 1980, were predominantly procedural. They did not deal with the ultimate question of whether such unlimited power should be given to five appointed individuals and a staff able to exercise their own political biases.

No amount of procedural reform can remedy the basic problem with the current FTC regulatory power. The fundamental problem is structural, not procedural: it is greater than assuring a complete factual record and procedural fairness. As the Administrative Conference of the United States, in its report that Congress had requested, stated: "when the underlying delegation of authority to an agency is as broad as that in Section 5 . . . hybrid rulemaking procedures are not an effective or efficient means of controlling agency discretion." The problem is one of having replaced the judgments of what is fair or unfair made by state legislators or Congress with the judgments of the staff and Commissioners of an administrative agency. This delegation of rulemaking power represents a complete restructuring of the relationships between the states and the federal government and between Congress and administrative agencies. It further represents an abandonment of some of the basic principles under which a democratic form of government arrives at major social policy decisions.

The basic problem is that as a legal standard, the work "unfair" gives little, if any, guidance. Traditionally our system of government has attempted to formulate and impose laws, and thereby define what is considered "fair," only after a majority consensus of the public is expressed through elected representatives. Legislatures have especial competence to make far-reaching judgments of this sort, for the democratic process is sensitive to the interests and desires of diverse segments of the American public in determining ultimate value judgments. Delegating determinations of "fairness," where major policy goals are at stake and objective standards are lacking, to a five-member commission insulated from the political process, is an abrogation of our democratic traditions.

In some contexts, where an agency is engaged in detailed implementation of a specific Congressional policy, the lack of public accountability characteristic of an administrative agency may properly be considered the price of efficient administration. A legislative body, while at its best in determining the direction of major policy, is ill-suited for handling masses of detail, or for applying general policy to the continuing and evolving problems that will be affected by the analysis of scientists or other professional advisers. No doubt exists, for example, that once a specific Congressional policy is established, the process of formulating rules on consumer matters that implement those policies may present very complex and detailed problems with which an administrative agency can deal most effectively. The broad determination of what conduct is "unfair" with respect to virtually all types of consumer transactions, however, does not present a case of implementing a specific policy. What is "fair" in the infinity of relationships and transactions between business and consumers involves the broadest social and political judgments. These are precisely the determinations of major policy that must be reserved for the legislative branch. To delegate such determinations to the FTC is to subordinate democratic principles of lawmaking to what can only be characterized as authoritarian, centralized lawmaking.

B. Existing checks on the FTC's rulemaking power are inadequate

Existing safeguards against abuse of the FTC's power to promulgate rules regulating unfair acts and practices are threefold: (1) a two-house post-rulemaking veto by Congress included in the 1980 amendments to the FTC Act; (2) provision for judicial review of all industry wide trade regulation rules finally adopted by the FTC; and (3) self imposed restraints in the form of FTC policy statements explicating the scope of its unfairness jurisdiction. None is adequate.

The legislative veto provides that all final rules promulgated by the FTC shall not become effective until they are submitted for review, and subject to possible disapproval through a joint resolution, by Congress. While the veto provides Congress with a mechanism to block any FTC rule that it chooses, its effectiveness is questionable in two respects.

First, there is considerable uncertainty as to the constitutionality of this device. Although the U.S. Supreme Court has not spoken on the issue, the U.S. Courts of Appeals for the Ninth and the D.C. Circuits—in *Chadha* v. *Immigration and Naturalization Service* (634 F.2d 408 (9th Cir. 1980)) and *Consumer Energy Council of America* v. *Federal Energy Regulatory Commission* (No. 80-2184, No. 80-2312, Slip Opinion (D.C. Cir 1982)) respectively—have held legislative vetos to be unconstitutional.

A second concern is its post hoc nature. The veto is exercisable only after adoption by the FTC of a rule. Experience shows that the cost incurred by both government and the private sector in the promulgation of any particular FTC trade regulation rule is substantial, and indeed may run into millions of dollars. An example is the Credit Practices Rule, which is still surrounded by controversy, despite numerous hearings, voluminous public comment, and enormous expenditures of time and money by the FTC and the private sector over a span of nearly 7 years of formal rulemaking proceedings.

Although all FTC trade regulation rules and all FTC orders on "unfair" acts and practices are subject to judicial review, the courts have not developed meaningful standards or criteria for defining the concept of unfairness. Rather, they generally defer to the FTC's expansive interpretation of its own enabling statute. Institutionally, the FTC in its role as prosecutor and enforcer has an incentive to interpret the statute in the broadest possible way and thus in its role as a lawmaker has an incentive to expand its jurisdiction. Deference to the FTC on questions of the meaning and scope of the unfairness standard renders the check on FTC power provided by judicial review largely illusory.

Despite FTC assertions to the contrary, the selfimposed standards for defining unfairness promulgated by the FTC are not adequate to guide agency discretion, nor are they likely ever to be adequate. The FTC has a vested interest, as lawmaker and judge, in interpreting section 5 in an expansive way. Consequently the FTC has not formulated and consistently applied criteria that narrow the language of the statute. It is hardly surprising, therefore that, in all of its numerous policy statements on the meaning of "unfairness," the FTC has never once given an example of conduct which is beyond the reach of the statute. The restraints on overly expansive FTC lawmaking must come from a source external to the FTC—the Congress.

In a 1980 policy statement the FTC held out three criteria historically applied by it in determining unfairness. Unfortunately, the FTC has not in fact applied the standards to develop a corpus of law to define what conduct was or was not fair.

Instead, the evidence of recent rulemaking proceedings, and statements of FTC officials, suggest that this policy standard has had little influence in determining "unfairness," and that the FTC believes its authority extends to areas which might not satisfy these criteria. Furthermore the FTC can weight these vague criteria as it chooses. For example, while the FTC takes the position in the 1980 statement that a "well established" public policy condemning a particular act or practice may be sufficient in itself to support a finding of fairness, the FTC also states that a well established public policy confirming the propriety and legality of a particular act or practice does *not* prevent a finding of unfairness.

C. The FTC rivals Congress and overshadows the States

The delegation of carte blanche rulemaking authority to the FTC is especially troublesome because of its implications for the erosion of Congressional power and the power of the states. Although the 1980 amendments to the Act included a legislative veto, the veto power does not provide any policy directions to the FTC, but merely allows Congress to disapprove FTC formulations of policy. The Congress, however, and not the FTC, has the especial competence to make basic policy determinations initially. The arrangement thus effectively shifts power which properly belongs to Congress to an administrative agency.

The impact on the proper relationship between state and federal governments is even more pernicious. Traditionally, states have had the responsibility for legislation in the area of commercial law, and the federal government has intervened only where some overriding federal policy indicated the matter could not be left to determination by purely local interests. The present Administration is dedicated to restoring a proper balance between the powers of the states and federal government. Yet, the FTC may now overrule state policies if in its sole discretion it considers some act or practice to be "unfair," even though state constitutions, legislatures, courts and agencies have policies to the contrary. It should be clear that allowing an administrative agency to overrule the legislatures and courts of the several states on questions of social policy that have traditionally been left to the states represents a fundamental restructuring of the relationship between state and federal government.

A ready example is provided by the FTC's Holder in Due Course Rule. Without discussing the merits of that Rule, it is sufficient to point out that the holder in due course principle is not one that had suffered from any neglect in state legislatures or judiciaries. In the years preceding the adoption by the FTC of its rule, the states paid a great deal of attention to the issue. Yet the FTC's resolution of the issue was at considerable variance with almost all of the legislative pronouncements and positions then existent, notwithstanding that the FTC has repeatedly stated that existing public policy is one of the major factors to be considered in determining unfairness. This disparity between well established public policy and the FTC's proposed rule suggests strongly that, rather than implementing legislative policy, the FTC in fact acted in disregard of it, sweeping away many years of careful study and progress by legislators, economists, legal scholars, and others, and dictating an immediate and rather profound effect in the law based on one thing: a willful assumption that the few individuals at the FTC who were involved in the rule's formulation knew best what was fair, and that the principles articulated by legislators throughout this country were therefore unfair, by definition.

All areas of commercial law are subject to similar attack by the FTC. What makes this particularly disturbing is the FTC's potential effect on carefully drafted, comprehensive state law, such as the Uniform Commerical Code. The U.C.C. is one of the significant success stories in the legal history of our nation. An impressive level of excellence and national uniformity of law has been achieved through the U.C.C. Thus, FTC rules which preempt the U.C.C. manage to collapse and scramble an extraordinary number of lines of definition and coordination which have laboriously been developed by the state legislatures, the National Conference of Commissioners on Uniform State Laws, the American Law Institute, and literally thousands of lawyers and judges who have been giving due regard to the many intricate considerations which make Code law understandable and workable. The spectre that five appointees in Washington, guided only by what their consciences dictate as "fair," can effectively nullify what it took some of the best legal minds in the country, in conjunction with the diligent efforts of countless legislators, a quarter century to produce, is troublesome indeed.

D. FTC staff and Commissioners ought not to have the power to make broad value judgments for our society

The determination of what is "unfair" by the FTC may simply not be a reflection of what is best for consumers or business. Regulation is costly, both in terms of compliance and in terms of the rulemaking process itself. Most often, industry compliance costs are simply passed through to the consumer. Frequently one class of consumers will receive a benefit and another class of consumers will be required to pay. The precise nature of the particular effort to protect consumers must be tested against broad policy goals, not merely immediate or narrow goals. Such an evaluation should be determinative of whether the net results are beneficial generally, and therefore whether the effort is sound. Bureaucrats, insulated from the political process, may not be sensitive to broader social policy alternatives: they may lack the perspective to assess the differential impact of the proposed rule across the consuming public. The entire population may end up paying high costs for a rule that benefits only a few.

Costs imposed by a regulation that outweigh benefits achieved work a severe hardship on consumers and business alike. Such costs contribute directly to inflationary trends in the economy. Ultimately the regulator gives the consumer less for his dollar under the guise of protecting him. Similarly, business wastes time and resources on compliance with needless regulation which could be better put to use in the improvement of consumer products and services. Such a result is intolerable and can only serve to undermine people's confidence in government. And rightfully so. The public has been daily becoming more aware of the powerlessness of its position as prices have risen over the last decade, in part because of over-regulation.

As Professor Louis Jaffee of Harvard, one of this country's leading administrative law scholars, has eloquently warned: "The notion so sedulously cultivated by many of us during the New Deal days that agencies, because they were expert, could go on spinning out of their own guts a continuing series of miraculous solutions was an absurd and a historical illusion. The stuff of great public policy controversies is basically political and can only be solved in the political arena."

III. AN APPROPRIATE ROLE FOR ADMINISTRATIVE AGENCIES IN CONSUMER PROTECTION: THE NEED FOR REFORM

Legislative rulemaking power is usually granted to agencies with regulatory jurisdiction over one specialized industry or over a narrowly defined segment of human activity that may cut across industry lines. Because their jurisdiction is narrowly defined, such agencies are able to develop an economic, sociological, and technological expertise regarding the particular activity regulated. Familiar examples include the Securities and Exchange Commission, the Federal Communications Commission, the Interstate Commerce Commission, the Federal Power Commission, and the Civil Aeronautics Board. The FTC represents a marked contrast to those agencies. Its jurisdiction ranges over all industries and issues except those specifically exempted. Because of the breadth of its jurisdiction, the FTC has an intimate knowledge of and expertise in very few industries. This lack of expertise in turn increases the likelihood of inadequacies in obtaining data, or errors of judgment, and of disruptions of entire industries due to poorly conceived or drafted rules.

Further, agency rulemaking authority is usually, and properly, circumscribed by well defined legal standards which give effect to particular policy goals identified by Congress. The unfairness standard is extremely open ended, vague and imprecise. As a result, under this standard, it is the FTC and not Congress which actually determines which policy goals to pursue.

Congress must first establish a basic policy. It may then choose to delegate rulemaking authority to implement that basic policy. A good example of how rulemaking power may be more appropriately apportioned between the Congress and the FTC in consumer matters is provided by the Equal Credit Opportunity Act. Congress made a basic policy determination that it was socially beneficial to prohibit discrimination on certain bases including race, color, religion, and sex, notwithstanding that the result might be an increase in the cost of credit. Congress then delegated to the Federal Reserve Board the power to enact regulations to fill in the interstices in the statute's language, resolve any ambiguities in the operation of the statute, allow for resolution of detailed problems, and provide a capacity for a rapid response to shifting problems within the parameters established by Congress.

A similar structure might be readily adopted in other areas affecting consumers that are of concern to Congress. For example, if Congress should decide that regulation of packaging or advertising of consumer products is advisable, it might enact legislation to establish general requirements in those areas, and then delegated to the Federal Reserve Board under the Equal Credit Opportunity Act to create rules to implement that specific legislation. In fact, Congress has already granted the FTC such authority in specific statutes, such as the Wool Products Labeling Act, the Textile Fiber Product Identification Act, the Fur Products Labeling Act, the Flammable

Fabrics Act, and the Fair Packaging and Labeling Act. The delegation of substantive rulemaking power to the FTC, within well-defined boundaries and in conjunction with specific guidelines, is the proper approach to an effective rulemaking role for the FTC.

In marked contrast, the FTC functions today with no policy guidance from Congress and with no limit on the subject matter in respect to which the Commission can legislate.

CONCLUSION

For the reasons set forth above Congress should repeal its grant of legislative authority to the FTC given under Section 18 of the Magnuson-Moss Act. After that repeal, delegations of supplemental rulemaking power to the FTC should be made only within the context of express statutory policies that are adopted by Congress.

Senator KASTEN. First of all, I would like to thank you, Mr. Carty, for not discussing or at least deferring comment on the antitrust issues. I think that that is correct at this time.

You mentioned your support for the renewal of the legislative veto provision, and I would like to know, Mr. Blum and Mr. Brandel, do you have positions on the legislative veto?

Mr. BLUM. We have in the past supported the concept of legislative veto. I see no reason why we should not in the future.

Senator KASTEN. Mr. Brandel.

Mr. BRANDEL. The Consumer Bankers Association has also supported the legislative veto.

Senator KASTEN. Mr. Carty, one criticism that has been leveled at FTC rulemaking is that a challenged practice is not sufficiently prevalent in the industry to justify industrywide rules. In other words, that an unlawful practice will just be spotty, and all of a sudden we end up with a huge rule. What is your view? Should a new standard be written into the law that would require some degree of industrywide participation in certain kinds of practice, a requirement that, in fact, the practice be prevalent in the industry in order to justify some kind of a rule?

Mr. CARTY. Yes; in fact, in the 1980 Improvements Act, as Senator Ford knows, the Senate version had a provision which required a prevalency test on proposed trade reg rules. I think an example of where the Commission has proposed a trade reg rule, and they have not met a prevalency test, is in the standards rulemaking proposal where they have come up with an example of a few violations of the antitrust laws versus over 20,000 standards.

We feel that this is an example of where they were trying to paint a whole industry or whole sector of the economy with the examples of a very few in comparison to the total number of standards out there, and we think a prevalency test is needed. And we feel that the language that Senator Ford had in the Improvements Act, which unfortunately was dropped out during the conference would be a good starting point.

Senator KASTEN. Senator Ford.

Senator FORD. About the only problems we have had basically is the legislative veto provisions. I have been opposed to legislative veto on the basis that we ought to have oversight, we ought to change the law, rather than sit here and give agencies carte blanche and then say no. I think you ought to cut the head off before you cut the tail off.

I am still opposed to legislative veto. We yielded, Mr. Brandel, to a two-House veto in the last bill. And I think it was Will Rogers that said that "nobody wants to rock the boat." What this country needs is a good boat rocker, and I hope that we are not afraid to rock the boat because we now have a Commission that is basically what we want.

I am hopeful we will go in and do the things that are necessary to protect the consumer, and give the businessman an idea of what to expect so everyone will not be jockeying from one administration to another, or from one session of Congress to the next. I would like to see some stability, therefore, that encourages me to have a little more interest in the legislation at this time than it may appear.

On that basis, I think it is time for those of us who have an interest in changes other than legislative veto look at the law itself and not worry about legislative veto.

Mr. Blum, you are opposed to the exemption of the professions. Is that correct?

Mr. BLUM. That is correct, Senator.

Senator FORD. Should there be any deference to the licensing boards in the States? I may have a problem here because having been a Governor, we set up these boards, and consumer protection agencies. We worked hard at the local level.

You could see, feel, and understand the problems, but then someone up here in Washington gets a letter and they dispatch someone who does not understand the community, does not understand the State, and does not understand the region.

Is there an area in which you say the States can regulate? As I asked the chairman awhile ago, how far may they go before the FTC takes over?

Mr. BLUM. Senator, I think the view of the small business community would not be so much that the State should not have a regulatory role, but rather, it would be a very Draconian solution to what you view as overregulation by precluding——

Senator FORD. What would you call Draconian?

Mr. BLUM. Precluding the Commission from having any regulatory authority over the State professional groups or any group that is regulated by the States. Small business, for example, is a user of health services, legal services, realtors, and the like. And I see no reason why the Commission should not maintain their jurisdiction if necessary to act in cases where there are restraints of trade and indeed, where restraints of trade transcend State borders and may be regional in nature.

Senator FORD. Would you be willing to see in this language a delineation of where the FTC would take over, where it would have an opportunity to preempt State licensure boards?

Mr. BLUM. In the question of purely intrastate activity I think the Commission does not act. If it is a purely intrastate action and it is the licensing board's responsibility to pass on the quality of services, I would probably view—I am speaking personally because we have not discussed this internally at the SBLC—it does not mean the Commission's role to pass on the quality of service as you discuss——

Senator FORD. Go ahead.

Mr. **Blum**. I think what we are dealing here with is a possibility that if you preclude the Commission from acting, that you potentially have a problem in the area of regional restraints of trade or, indeed, we are having nationwide involvement of realtors, financial services, we are getting more of a trend to integration in a lot of different service-rendering professions.

And I think that if you except the FTC—if you preclude the FTC from getting involved in restraints of trade by these groups, the States are not going to have the resources to be able to deal with them.

Senator **Ford**. Well, we have the "new federalism." It is going to cost the states $15 billion, I guess a little bit more will not hurt.

We have a bill before us that has a State-action provision. Are you aware of that bill with that State action provision in it?

Mr. **Blum**. Are you talking about the bill by Senators McClure and Melcher?

Senator **Ford**. No, Senator Cannon's bill.

Mr. **Blum**. I am aware of the bill, Senator. I have not read it.

Senator **Ford**. Would you, and all of you, look at the State-action provision that Senator Cannon has in his bill. I would hope you would have a chance to do that. I understand my time is up, Mr. Chairman. I do have one more question I would like to ask when I get some more time.

The **Chairman** [presiding]. Go ahead.

Senator **Ford**. I just have one other question to Mr. Brandel. You talked about having a balance between the States and the Federal Government. What would you perceive as a good balance between the States and the Federal Government?

Mr. **Brandel**. Well, Senator Ford, I think that balance———

Senator **Ford**. You wanted a balance between the States and the Federal Government?

Mr. **Brandel**. That is correct. The institution to decide that proper balance is the Congress. It is not a five-man appointed agency. That is the thrust of the Consumer Bankers Association's position. There will constantly be shifts of power between the States and the Federal Government, but at the moment the decisions are taking place in an administrative agency, not where they belong: in this Congress.

I wonder if I might amplify our position with respect to the legislative veto. That provision was supported because the Congress appeared to be unwilling in 1980 to do directly anything about the FTC's unlimited power to make law, not because it was viewed as the best solution.

The legislative veto, as you well know, is in trouble before the judicial system. It has been found unconstitutional by both the ninth circuit in *Chadha* v. *Immigration and Naturalization Service* and by the Court of Appeals for the District of Columbia in *Consumer Energy Council of America* v. *Federal Regulatory Commission.* The opinion in the Court of Appeals decision for the District of Columbia was exhaustive. In response to claims by counsel for the House and the Senate, that the legislative veto was necessary in order to prevent excessive Presidential and regulatory agency power and discretion, the court closed with an insightful statement. The court said: "The great irony in this view is that there has been no use of rulemaking power by either the President or unelected independent administrators. Their powers have come solely from congressional authorizations. If Congress has given away too much power, it may by statute take it back or may in the future enact more specific delegations." That is precisely what we think the Congress ought to do.

The CHAIRMAN. Gentlemen, I have no questions, but Wendell, I wish you would not talk about rocking the boat. I am sensitive on that subject. [Laughter.]

Senator FORD. I do not understand. What do you mean? [Laughter.]

The CHAIRMAN. Gentlemen, thank you very much. We will start again at 9:30 in the morning.

[Whereupon, at 11:21 a.m. the subcommittee was recessed, to reconvene at 9:30 a.m. the following day, Friday, March 19, 1982.]

REAUTHORIZATION OF THE FEDERAL TRADE COMMISSION

FRIDAY, MARCH 19, 1982

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, D.C.

The subcommittee met, pursuant to recess, at 9:30 a.m., in room 235, Russell Senate Office Building, Hon. Robert W. Kasten, Jr., presiding.

OPENING STATEMENT BY SENATOR KASTEN

Senator KASTEN. Welcome to our second of 2 days of hearings on Federal Trade Commission authorization and oversight. Yesterday, we heard from Chairman Miller, and we had one panel of public witnesses. Today we have a full schedule with three more panels. The first panel will focus generally on the FTC's consumer protection authority, the second will focus on regulation of commercial advertising, and the third will be on the legislative veto.

Each member of the panel will be given a limited time for a summary of his statement. I might remind everyone that the full text of all the statements will appear in the record if they will summarize them. Then we will begin rounds of questions from members of the committee.

All three panels include witnesses with different viewpoints, so we are looking forward to lively discussions. Witnesses should feel free to respond to questions directed to any of the other panelists, because frankly, what we want to do is collect as much information on differing views as is possible.

Our first panel is made up of Mr. Martin Connor, Mr. Mark Silbergeld, Mr. John Montgomery, Mr. James Delong.

Mr. Connor.

STATEMENTS OF MARTIN F. CONNOR, CHAMBER OF COMMERCE OF THE UNITED STATES; MARK SILBERGELD, DIRECTOR, CONSUMERS UNION; JOHN T. MONTGOMERY, CHIEF, CONSUMER PROTECTION DIVISION, DEPARTMENT OF THE ATTORNEY GENERAL OF MASSACHUSETTS; AND JAMES V. DELONG, ATTORNEY

Mr. CONNOR. Thank you, Mr. Chairman. My name is Martin Connor. I am a Washington corporate counsel for General Electric Co. and I am a member of the chamber's council on antitrust policy. The chamber has submitted a very full written statement which deals with both the antitrust and consumer protection aspects of the Federal Trade Commission's activities.

The statement was prepared quite some time ago, Mr. Chairman, before we learned that it was your intention in these hearings to address only consumer protection issues. In my very brief oral summary of the chamber's position, I will constrain myself to that subject.

Senator KASTEN. Thank you.

Mr. CONNOR. Two years ago, Congress enacted the Federal Trade Commission Improvements Act of 1980 which contained new agency procedures and a variety of restrictions on certain pending proceedings.

The chamber, to begin with, supports continuation of several aspects of the 1980 legislation including limitations on intervenor funding, prohibition of unfairness rulemakings with respect to commercial speech, and periodic congressional oversight of the Commission. At the same time, the chamber urges Congress to address on a more comprehensive basis the FTC's basic section 5 authority.

The FTC's openended unfairness mandate has led the agency in recent years into a series of widely criticized proceedings in both the antitrust and consumer protection areas. Quite a few of these are discussed in the chamber's written statement.

In the chamber's view, it is time for Congress to clarify section 5 of the Federal Trade Commission Act and to set the Commission on a course which has been clearly charted by the Congress.

The chamber proposes that the Commission's authority to address unfair or deceptive acts or practices be defined in terms of the principles that were set out in the Commission's December 17, 1980 letter to Senators Danforth and Ford, and in its March 5, 1982 letter to this committee.

I think that in the little time I have here, probably the most useful thing I could do for the committee would be to compare the chamber's position in this regard with the position that it heard yesterday from Chairman Miller, who also endorsed the application of these principles to the Commission's unfair acts or practices activities.

As you will note, the chamber takes the position that these same principles should be applied in the case of both unfair and deceptive acts or practices. The chamber agrees with the position taken yesterday by Mr. Miller that the committee would not do enough to address simply unfair acts or practices. We agree with the analogy he drew of the balloon that if you squeeze the unfairness end of the balloon it will tend to come out at the deceptive end.

The chamber, therefore, recommends that the same principles be applied in each case except in cases involving classic commonlaw deception that is deliberate, a falsehood or reckless disregard for truth. The Commission has not actually often distinguished between what is unfair and what is deceptive.

As Senator Danforth remarked yesterday, until the early 1970's all of the Commission's consumer protection activities were undertaken under the rubric of deception. Encouraged by the 1972 Supreme Court decision in the S&H Green Stamp case, the Commission then, in a series of cases, began to use both theories—unfair, alleging that conduct was unfair, and that it was also deceptive. But the Commission has very rarely, very rarely, brought actions, particularly rulemaking actions, alleging that conduct was simply unfair or simply deceptive.

A couple of examples might illustrate this point. The FTC's eyeglasses rule was brought strictly on an unfairness theory. The Commission's used car dealer rule was brought—the eyeglasses was on an unfairness theory. The used car dealer rule was on a deception theory.

The point is, though, whatever the theory, whether unfairness in the one case or deception in the other, the rationale was the same. The Commission was alleging that information had been withheld from the consumer. In fact, the Commission and the two notions are interchangeable. In fact, oftentimes, the Commission has simply fudged the difference.

It is very typical for a Commission rule or proposed rule to begin as the product standards rule began. It is an unfair method of competition and an unfair or deceptive act or practice to violate any applicable provision of this rule. Whether the Commission was addressing an unfair practice or a deceptive practice was completely fudged.

In the statement which the staff sent to the Commission on September 20, 1978, asking them to propose this rule, the staff said this: A number of the acts and practices intercepted by the rule could easily be double-pleaded under traditional Commission competition and consumer protection theories. Several theories of competitive and consumer injury have been developed. Staff considered it particularly important to lay a clear foundation for double-pleading.

In other words, they are covering all bases. For these reasons, the chamber has concluded that to simply address unfairness to the exclusion of deceptive acts or practices, you know, would be inadequate. We would propose, therefore, that the test of direct injury to the consumer, as laid out in the 1980 policy statement, be made applicable both to unfair and deceptive acts and practices.

We also recognize, however, that not every consumer injury should be actionable, and therefore, again consistent with the 1980 and 1982 letters, the consumer proposes that consumer injury first should be substantial; second, that it should be an injury which the consumer himself or herself could not reasonably have avoided, and third, that it be an injury which is not outweighed by benefits to consumers or to competitors.

On this last point, I would like to mention that we are not asking for elaborate cost-benefit analysis, but simply for an informed judgment that consumer injury is not offset by consumer benefit.

I would also point out that in many cases, particularly the common law types of deception, there would be no question of consumer benefit. The issue would not even arise.

Finally, the chamber proposes two additional modifications to section 5. First, in order to focus the FTC on commercial practices rather than health and safety matters, the chamber's proposed legislation would preclude FTC consumer protection proceedings which intrude into the jurisdiction of other, more specialized regulatory agencies. We have in mind specifically such agencies as CPSC, NTSA, and EPA.

Second, the chamber calls for a repeal of section 5(m)(1)(b), a procedural provision which we believe contrary to fundamental provisions of due process.

Thank you very much.

[The statement follows:]

STATEMENT OF MARTIN F. CONNOR ON BEHALF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES

Mr. Chairman and members of the Subcommittee, my name is Martin F. Connor. I am Washington Corporate Counsel of the General Electric Company and also a member of the FTC Subcommittee of the U.S. Chamber's Council on Antitrust Policy. We on the Subcommittee are responsible for assisting in the development of the Chamber's position on issues affecting the Federal Trade Commission. Accompanying me today is Fred Byset, the Chamber's Associate Director of Government and Regulatory Affairs for Antitrust.

The Chamber of Commerce of the United States is the world's largest business federation of corporations, trade associations, chambers of commerce and individuals engaged in business and the professions. On behalf of our more than 225,000 members, we greatly appreciate this opportunity to share our views on the proper role of the Federal Trade Commission in our competitive economy.

In the Chamber's view, Congress, and this Committee in particular, should act affirmatively to chart the future course of the Commission's administration of Section 5 of the FTC Act. Although widely criticized in recent years, the FTC has a useful role in enforcing the nation's antitrust laws and in protecting the individual consumer against commercial misconduct. The scope of this role, however, should be more precisely defined by the Congress and not be left to the discretion of the individuals who at any given moment constitute the Commission. While the Chamber applauds the emphasis on economic analysis and the respect for market forces brought to the Commission by Chairman Miller and his staff, we cannot ignore the prospect that those contributions may be nullified in the future. We therefore urge the Congress to provide more certain guidance to all future Commissions and to the courts which will review their actions.

Under its vague and undefined Section 5 "unfairness" authorities, the FTC has claimed vast and potentially arbitrary power to intervene broadly in the market. While FTC orders are subject to judicial review, the elusive nature of the "unfairness" concept gives the courts no standard by which to assess the validity of FTC action. Thus, the courts have been largely relegated to a limited review of evidentiary and procedural issues. Generally, as long as the Commission follows prescribed procedures and marshalls some evidence of record to support its position, the ultimate conclusion as to what does or does not "violate" Section 5 is effectively insulated from judicial scrutiny.

Given these inherent limitations on court review under the existing statute, and the political pressure generated on the Commission by the vagueness of its own mandate, the need for Congressional action is immense. Congress bears the ultimate constitutional responsibility for FTC actions since the agency is wielding power delegated by statute. As the Commission itself has recently recognized, it is "entirely proper" for Congress to "provide as much guidance as feasible to administrative agencies" in the form of more precise statutory standards for the benefit of both the "regulated" and "regulator." [1] In the same manner, the Chamber also believes it both timely and appropriate for Congress to clarify the broad delegation under Section 5 and thus to set the Commission on a Congressionally-defined and bounded course.

A little more than two years ago, Congress undertook a review of the operations and policies of the FTC resulting in the FTC Improvements Act of 1980. At that time, the Commission, under different leadership, was pursuing regulatory initiatives which intruded into the affairs of industry and commerce from one end of society to the other. In the name of consumerism, the FTC was scrutinizing activities from children's advertising to funerals in an effort to provide cradle to grave protection, while in the area of broader economic regulation, it claimed Section 5 legal authority to restructure entire industries, without antitrust violation, to meet its own notions of market structure and performance.

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[1] Letter of Comm., per Chairman Miller, to Senators Packwood and Kasten dated March 5, 1982 at pp. 8-9.

In response to this situation, the 1980 Improvements Act contained a variety of loosely related provisions ranging from specific restrictions on ongoing proceedings to new agency procedures. Some of the provisions were permanent in nature, while others—including many which the Chamber believes should now be made permanent—were effective for only a specific period. The 1980 legislation did not attempt to address the more fundamental problem inherent in the FTC's undefined and open-ended Section 5 mandate.

In recent months, the Chamber has given long study and careful thought to the directions this Congress might give the FTC. We have reviewed the various proposals advanced, and in many cases adopted, in connection with the 1980 Improvements Act and have come to the conclusion that reform must go beyond procedure and ad hoc review of individual proceedings. We believe that Congress must now take a hard look at the FTC's basic Section 5 authority in both antitrust and consumer protection and redefine the agency's power by enacting meaningful substantive standards in the governing statute.

The U.S. Chamber, in consultation with other leading business groups, has prepared draft legislation designed to achieve this objective which we now submit for this Committee's consideration. (See Appendix A hereto.) In our view, the concepts incorporated in this draft legislation could provide a sensible, long-term means for revitalizing the FTC in its legitimate regulatory sphere.

In the antitrust area, for example, the FTC's generally repudiated efforts at activist economic regulation reflected, to a large degree, confusion on the part of the agency as to its proper enforcement role. Not wishing merely to duplicate the activities of the Department of Justice and without meaningful guidance from Congress, the FTC during the 1970's began probing the outer bounds of its Section 5 "unfairness"/antitrust authority. This search for a specific mission, unfortunately, led the agency into a series of ill-conceived and adventurous proceedings, such as the cereal and automotive industry cases, which absorbed enormous Commission and private resources and raised widespread concern that the FTC regarded itself as a centralized economic planning agency.

The Chamber's proposed legislation is designed to return the FTC's Bureau of Competition to the mainstream of antitrust enforcement. It would require the agency to observe established Sherman Act principles in Section 5 cases and, in this way, would provide meaningful guidance to the Commission and to reviewing courts. The proposal would reemphasize the role of antitrust, with its focus on market freedom, as the major instrument of competition policy, foreclosing the pursuit of nebulous "social" objectives. In a larger sense, the Chamber's proposal contemplates a long-term accommodation between a Justice Department focused on *per se* offenses and an FTC focused on complex, rule of reason cases where administrative expertise and remedies are particularly appropriate.

Similarly, in the consumer protection area, the Chamber's proposed legislation incorporates specific standards to govern the FTC's exercise of its "unfair or deceptive acts or practices" jurisdiction. The proposal essentially leaves intact the FTC's authority to strike down falsehoods, reckless claims, or practices that are intentionally misleading. Such conduct has no place in our free enterprise system and the FTC, under the Chamber's draft language, would be fully empowered to prevent it.

When, however, the Commission moves beyond reprehensible conduct and seeks instead to attack business practices because of an alleged adverse impact on consumers, the Chamber's proposal would provide it with substantive guides to bring agency action within proper bounds. The Chamber believes that the Commission should intervene on an impact basis only when the alleged injury to consumers is substantial and not reasonably avoidable and then only when the benefits of government intervention outweigh the costs which such intervention would impose on consumers and the competitive systems. Significantly, these guideposts in the Chamber's proposal are the very same criteria that the FTC itself recommended, only two weeks ago, as appropriate elements in a more precise statutory definition of "unfairness."[2] The Chamber thus basically accepts the Commission's own formulation which, we believe, expresses the appropriate statutory limits of the agency's consumer protection jurisdiction.

Consistent with and complementary to our substantive proposal, the Chamber is proposing two additional modifications to section 5. First, we believe that the Congress should make clear to the FTC that its consumer protection jurisdiction does not overlap the jurisdiction of specialized regulatory agencies and should focus on commercial practices rather than health or safety problems. Second, we urge the repeal of Section 5(m)(1)(B) which authorizes the Commission to seek civil penalties against companies for violations of cease and desist orders entered without notice to them and without an opportunity for them to be heard. The costs of Section 5(m)(1)(B) clearly outweigh any possible enforcement benefit.

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[2] Letter of Comm., per Chairman Miller, to Senators Packwood and Kasten dated March 5, 1982 at pp. 7-9. Only Commissioner Pertschuk did not share the view of his fellow Commissioners that new statutory standards would be appropriate. Nonetheless, even he agreed that should Congress adopt new legislation concerning "unfairness," it should properly include the concepts of substantiality, unavoidability, and cost-benefit analysis.

I. CONTINUATION OF CERTAIN PROVISIONS OF FTC IMPROVEMENTS ACT OF 1980

As legislation arising in part out of the appropriations process, several of the provisions in the FTC Improvements Act of 1980 were tied to the expenditure of agency funds during designated fiscal periods. Therefore, absent congressional action, certain key aspects of the 1980 Improvements Act will expire at the end of the current fiscal year.

The U.S. Chamber strongly supported many of these provisions during the hearings leading up to the enactment of the 1980 legislation. The Chamber continues this support and urges that the provisions identified below be incorporated in the FTC's organic statute.

The reasons justifying the original adoption of these provisions in the 1980 Improvements Act are fully set forth in the hearings and debates that preceded that legislation and need not be repeated here. Experience during the last several years under the new legislation, however, has fully confirmed their appropriateness.

Specifically, the National Chamber believes that the following portions of the FTC Improvements Act of 1980 should now be made a permanent part of the FTC's governing statute:

1. *Intervenor Funding Limitations.* While the Chamber believes that all interest groups, and particularly consumers, should be represented in agency proceedings, Congress found that there had been serious abuses in the FTC's administration of intervenor funding, including selective disbursement to groups in agreement with the FTC's position, staff preparation of written statements for so-called "public" witnesses, and funding of unqualified individuals and groups. Congress adopted important safeguards in this area in the 1980 Improvements Act which should now be continued.

2. *Prohibition of "Unfairness" Rulemakings with Respect to Commercial Advertising.* The Chamber has consistently criticized the FTC's use of rulemaking to "legislate" broadly with respect to so-called "unfair" acts and practices. "Unfairness" is an elusive and amorphous concept which becomes even more tenuous when pursued in an unfocused rulemaking process. As the children's advertising and similar proceedings have demonstrated, "unfairness" rulemaking with respect to commercial advertising is particularly suspect and raises issues of constitutional dimension. Congress properly prohibited such activities in the 1980 Improvements Act, a prohibition that should not be incorporated on a permanent basis.

3. *Congressional Oversight.* The current authorization act contemplates regular Congressional oversight of the Commission, including pre-enforcement review and possible veto of the agency's rules. We supported this concept in the 96th Congress as an effective mechanism for insuring compliance with Congressional intent, and we urge renewal—not inconsistent with constitutional considerations and a proper balance of legislative and executive branch authority.[3]

While Congress should take prompt affirmative action with respect to each of these items, the Chamber does not believe that continuation of these 1980 Improvements Act provisions is a substitute for providing substantive content to the Section 5 standards and meaningful direction to the FTC in carrying out its antitrust and consumer protection missions.

II. CLARIFICATION OF THE FTC'S POWER TO PREVENT "UNFAIR METHODS OF COMPETITION"

The first important aspect of the Chamber's proposed legislaton concerns FTC antitrust enforcement under its Section 5 authority to prevent "unfair methods of competition." The Commission has operated under this broad and essentially unrestricted "unfair methods" mandate for almost seventy years. Although originally interpreted in a manner generally consistent with the mainstream of antitrust enforcement, this authority has been used repeatedly by the FTC during the last ten years to justify new programs of activist regulatory intervention in the nation's economy.

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[3] The Chambler also generally supports continuation of one other aspect of the 1980 Improvements Act, *i.e.*, limitations on FTC participation in trademark cancellation proceedings, which is also scheduled to lapse at the end of the current fiscal year. Trademark cancellation proceedings concerning whether a mark has become a "common descriptive name" can be exceedingly long and complex. In the Chamber's view, FTC involvement in such proceedings represents a waste of the Commission's scarce resources, especially as affected industry members already have a strong incentive to protect their own interests in such matters.

The crux of the problem is the absence in the statute of objective standards for determining what is and is not an "unfair method of competition." Because of this critical failure, the FTC has had relatively little meaningful judicial review and has often felt free to attempt to impose on the business community the policy preferences and social priorities of incumbent Commissioners and staff. Moreover, the lack of substantive limitations in the Commission's statutory authority has exposed the Commission to pressure to remedy any economic condition which a politically powerful faction regarded as an "evil."

The Chamber's proposed legislation would remedy this situation by incorporating into Section 5 of the FTC Act the established body of judicial precedent under Sections 1 and 2 of the Sherman Act. By thus directing the FTC to adhere to Sherman Act standards as defined by the Court, the Chamber's proposal would effectively eliminate the FTC's roving antitrust "unfairness" mandate.

A. THE NEED FOR OBJECTIVE STANDARDS FOR DETERMINING "UNFAIR METHODS OF COMPETITION"

In vesting the FTC in 1914 with jurisdiction to prevent "unfair methods of competition," Congress acted in the context of and in response to prior judicial decisions under the Sherman Antitrust Act. The Federal Trade Commission Act was enacted in reaction to the Supreme Court's adoption of the "Rule of Reason" standard for judging the legality of trade restraints under Section 1 of the Sherman Act. *Standard Oil Co.* v. *United States,* 221 U.S. 1 (1911). The *Standard Oil* decision was not well received in Congress where it was viewed as a weakening of the Sherman Act prohibitions. Accordingly, Congress invested the FTC with broad "unfair methods of competition" authority to counteract the perceived potential for judicial emasculation of the Sherman Act.[4]

Obviously, much has changed since 1914. Sherman Act enforcement has not withered away, but has instead evolved over the years a rich and substantial body of precedent which defines, with reasonable predictability, our national competition policy. Indeed, expansive judicial interpretations of pertinent Sherman Act doctrines[5] have made the statute a very powerful and adaptable weapon against all forms of anticompetitive abuse.

This evolution of Sherman Act principles has essentially mooted the original 1914 Congressional concerns that gave rise to the FTC's vague "unfair methods of competition" authority. At the same time, the intervening years—and especially the decade of the 1970's—have witnessed a series of dubious FTC proceedings that manifest the dangers inevitably created by an undefined and open-ended legislative mandate. These proceedings include:

1. "Shared Monopoly Cases" in which the FTC attacks industry structure arising, without collusion, in the market and seeks to reshape industries to meet the FTC's regulatory notions of optimum restructuring. The Chamber is acutely conscious that the *Cereal* case[6] ended in a precedential "draw" with three Commissioners refusing to foreclose a rerun in a more propitious political climate.
2. "Bigness is Badness Cases" in which the FTC attacks large companies on social grounds and seeks to limit their growth and efficiency advantages. The now terminated, but never legally repudiated, oil industry proceeding and automotive investigation are recent examples.[7]

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[4] *See* Averitt, *The Meaning of "Unfair Methods of Competition" in Section 5 of the Federal Trade Commission Act,* 21 B.C.L. Rev. 227, 228–38 (1980).

[5] *See, e.g., Interstate Circuit, Inc.* v. *United States,* 306 U.S. 208 (1939) (providing a very relaxed standard of proof for the conspiracy or combination element of Sherman §1); *United States* v. *Container Corp.,* 393 U.S. 333 (1969) (agreement to exchange price information invalidated under Sherman §1 despite minimal anticompetitive effect).

[6] *Kellogg Company, et al.,* 3 CCH Trade Reg. Rep. ¶21,899 (FTC Docket 8883), complaint dismissed by Order dated January 15, 1982 with separate or dissenting statements by Commissioners Clanton, Pertschuk and Bailey.

[7] *Exxon Corp., et al.,* 3 CCH Trade Reg. Rep. ¶21,866, (FTC Docket 8934), complaint dismissed September 16, 1981; *See* 3 CCH Trade Reg. Rep. ¶10,438 (reporting May 13, 1981 FTC press release that announced closing of five-year, industrywide antitrust investigation of the automobile industry).

3. "Noncollusive Parallelism Cases" in which the FTC attacks commercial practices arising pervasively, without collusion, in the free market and attempts to dictate better methods of doing business. The *Ethyl* case [8] now before the Commission is an example of this activity as was the earlier *Boise Cascade* (Plywood) case.[9]

4. "New Nonstatutory Offense Cases" in which the FTC attacks market practices which Congress specifically chose to exempt from antitrust coverage. In the *Times-Mirror* case, for example, the Commission seeks to use Section 5 to extend the Robinson-Patman Act to services not covered by that statute.[10]

5. "Competitive Balancing Cases" in which the FTC attacks market practices in one industry because they may distort the FTC's model of competition in another. Thus, the FTC's order in *Reuben H. Donnelley* (Airline Guide) attempted to restrict the discretion of the publisher to improve competitive balance in the airline industry. While that particular excess was overturned by the Second Circuit even under Section 5, the FTC continues to pursue similar theories in other proceedings.[11]

While this list is by no means exhaustive by category or case, it clearly illustrates the pressing need for legislation to provide substantive content to the FTC's "unfair methods" jurisdiction.

Equally significant, the lack of objective standards governing the FTC's antitrust enforcement also serves to insulate the agency from effective judicial review. Without Congressional guidance in the FTC's organic statute, the courts have traditionally given the FTC great latitude in proscribing trade methods under the elusive "unfairness" rubric.[12] Confining their review principally to substantial evidence and procedural fairness issues, the courts have thus been unable to curb effectively the FTC's attempts at activist regulatory intervention.

In sum, the premise upon which the 1914 Congress invested the FTC with its "unfair methods of competition" jurisdiction is no longer valid. The development and expansion of Sherman Act doctrine over the years has essentially eliminated the need for the FTC's elastic, catch-all "unfairness" mandate. At the same time, the lack of substantive content in the organic statute has allowed the FTC to engage in intrusive economic regulation at the whim of transient majorities and unchecked by meaningful judicial review.

B. THE EFFECT OF THE CHAMBER'S PROPOSED LEGISLATION ON FTC ANTITRUST ENFORCEMENT

The Chamber's proposed amendment to Section 5(a) provides substantive content to the statutory prohibition of "unfair methods of competition" in two ways. First, it adopts the established body of judicial precedent developed under Sections 1 and 2 of the Sherman Act. And second, it incorporates all of the categories of practices that Congress may specifically define to be unfair.[13]

The proposed amendment thus returns the FTC to the mainstream of antitrust enforcement. Instead of being guided only by its own fluctuating perceptions of "fairness," the agency will have to exercise its "unfair methods of competition" authority in accordance with the dictates of Congress and/or established Sherman Act principles as developed by the courts.

At the same time, the Chamber's proposal will not frustrate any legitimate antitrust enforcement objectives that Congress believes the FTC should pursue. Thus, the amendment will have no impact on the FTC's separate statutory authority to enforce the Robinson-Patman Act and Sections 3, 7 and 8 of the Clayton Act. Further, the amendment expressely confirms and preserves the FTC's long-recognized power to proceed against all Sherman Act violations.[14]

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[8] *Ethyl Corp., et al.*, 3 CCH Trade Reg. Rep. ¶ 21,856 (FTC Docket 9128), appeal from 8/12/81 Initial Decision finding Section 5 violation now pending before full Commission.

[9] *Boise Cascade Corp.*, 91 F.T.C. 1 (1978), *rev'd sub nom. Boise Cascade Corp.* v. *FTC*, 637 F.2d 573 (9th Cir. 1980).

[10] *Times Mirror Co.*, 3 CCH Trade Reg. Rep. ¶ 21,871 (FTC Docket 9103), consent order to cease and desist announced September 25, 1981 with Acting Chairman Clanton dissenting. *See Perpetual Federal Savings & Loan Ass'n*, 90 F.T.C. 608, 648 (1977), *order withdrawn*, 94 F.T.C. 401 (1979), in which the FTC attempted to use Section 5 to extend Clayton Section 8 and exercise jurisdiction over Bank-S&L director interlocks.

[11] *Reuben H. Donnelley Corp.*, 95 F.T.C. 1 (1980), *rev'd sub nom. Official Airline Guides* v. *FTC*, 630 F.2d 920 (2d Cir.), *cert. denied*, 101 S.Ct. 1362 (1981). *See Ford Motor Co.*, FTC Docket 9113, and *General Motors Corp.*, FTC Docket 9114, in which the FTC has attacked under Section 5 automobile manufacturers' business judgment in purchasing advertising in order to improve competition in rental and leasing industry.

[12] *E.g., FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233 (1972) (upholding FTC's authority to make ad hoc judgments of "fairness" concerning practices which violate neither the letter nor the spirit of the antitrust laws).

[13] Congress has already defined a number of acts and practices to be "unfair methods of competition" in the Wool Products Labeling Act (15 U.S.C. § 68 *et seq.*), the Fur Products Labeling Act (15 U.S.C. § 69 *et seq.*), the Fur Products Labeling Act (15 U.S.C. § 69 *et seq.*), the Textile Fiber Products Identification Act (15 U.S.C. § 70 *et seq.*). The Chamber's proposed amendment would carry forward such definitions without the need for further conforming changes.

What the proposed amendment does eliminate, however, is the potential for agency abuse that currently exists under the vague and otherwise contentless "unfair methods of competion" language. In particular, the amendment will prevent future FTC excesses based upon the so-called "incipiency," "spirit," and "*S&H* public values" theories.

Under the "incipiency" doctrine, the FTC claims the authority to stop acts and practices which, when full blown, would violate the Sherman and Clayton Acts.[15] How close to a completed violation a respondent must be before this incipiency theory can apply, however, is completely undefined. While such an approach may have made sense in 1914 when the reach of the Sherman Act was in doubt, today this doctrine provides the FTC carte blanche to attack legitimate, procompetitive business conduct based on mere speculation as to future developments. Current interpretations of Section 1 of the Sherman Act already provide a means to redress facilitating practices that might lead to trade restraints, while both the "conspiracy to monopolize" and "attempt to monopolize" provisions of Section 2 of the Sherman Act can be used effectively to halt anticompetitive behavior at an early stage. Accordingly, elimination of the open-ended "incipiency" theory under FTC Act Section 5 will reduce the potential for abuse that now exists without sacrificing any legitimate enforcement objective.

In the same manner, the so-called "spirit" application of Section 5 under which the FTC may "fill in the gaps" and prohibit conduct that violates the "spirit" or policy, but not the letter, of other antitrust laws is both largely unnecessary and subject to misuse. The Sherman Act, as it has evolved over the years, provides adequate authority to prevent unreasonable restraints of trade and fully embodies a policy of free and open competition. The undefined "spirit" doctrine permits the FTC to ignore specific statutory and/or judicially prescribed elements and, in effect, to create entirely new substantive offenses. If any "gaps" in fact exist which need to be "filled in," such a task is best left to the Congress.

Finally, the proposed amendment would effectively overrule the Supreme Court's suggestion in the *S&H* case[16] that the FTC can procribe conduct as an "unfair method of competition" based solely on unarticulated and undefined "public values," even though such conduct poses "no threat to competition within the precepts of the antitrust laws" (405 U.S. at 244-45). Such overbroad delegation of discretionary authority, by its terms, has nothing to do with legitimate competition policy and smacks instead of centralized economic planning.

In summary, the Chamber's proposed amendment will not affect the FTC's traditional jurisdiction to enforce the Sherman, Clayton and Robinson-Patman Acts. It will, however, appropriately define the boundaries of such jurisdiction and preclude the FTC from regulating legitimate business conduct based solely on the agency's own peculiar "fairness" notions.

C. THE FTC'S ANTITRUST ENFORCEMENT ROLE UNDER THE CHAMBER'S PROPOSED LEGISLATION

The Chamber strongly supports soundly administered antiturst enforcement. Since its inception, the FTC has shared concurrent enforcement jurisdiction with the Department of Justice to redress Sherman Act and other antitrust violations. While this situation will continue under the Chamber's proposed legislation, the FTC's role in antitrust enforcement need not merely duplicate the Justice Department's efforts. Indeed, the Chamber's proposal will lay the foundation for a sensible long-term division of Sherman Act responsibilities between these two agencies.

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[14] *E.g., FTC* v. *Beech-Nut Packing Co.*, 257 U.S. 441, 453 (1922) (Sherman Act is "declaration of public policy to be considered in determining what are unfair methods of competition"); *FTC* v. *Cement Institute*, 333 U.S. 683, 690 (1948) (expressly holding that FTC may condemn and suppress Sherman Act violations under FTC Act Section 5.)

[15] Such "incipiency" authority has been recognized by the Supreme Court. *E.g., FTC* v. *Cement Institute*, 333 U.S. 683, 693 (1948); *FTC* v. *Motion Picture Advertising Service Co., Inc.*, 344 U.S. 392, 394-95 (1953). In doing so, howeve[illegible] Court indicated that it was executing the clear legislative intent of the 1914 Congress. *See e.g.,* MacIntyre & Volhard, "The Federal Trade Commission and Incipient Unfairness," 41 Geo. Wash. L. Rev. 407, 414-15 (1973). In 1914, of course, there was a perception that the Sherman Act's proscription of monopoly and trade restraints was in danger of being judicially weakened—a perception that subsequent developments have proved to be unfounded.

[16] *FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233 (1972).

Enforcement activity by the Antitrust Division tends to focus principally on "hard core," *per se* types of violations. Only the Justice Department can seek criminal sanctions under the Sherman Act and the Department has recognized a responsibility to devote a substantial portion of its resources to the pursuit of criminal anticompetitive conduct. The Department is thus somewhat constrained in undertaking litigation of the more complex, economically-oriented issues that can arise under a full-scale rule of reason analysis.

Under the Chamber's proposed amendment to Section 5, the FTC's enforcement efforts can appropriately complement the Justice Department's activities and be channeled toward areas where the agency's expert economic resources will be most profitably utilized. The FTC will be able to undertake a detailed reexamination of the economic underpinnings of various antitrust theories and help rationalize this area of the law. Similarly, the FTC can bring enforcment actions under established Sherman Act standards to test the competitive effects of new business practices and conduct as they emerge. In such cases, where the practice at issue is either completely new or perhaps previously untested, the cease and desist remedies available to the FTC, which operate only prospectively, are particularly appropriate.[17]

The Chamber's proposal also provides inherent flexibility that will allow the FTC and Congress to work together to ensure that national antitrust objectives are fully realized. To this end, the proposed amendment contemplates that Congress, based on the recommendations and analyses of the FTC, can statutorily define any new category of conduct to be an "unfair method of competition." In such cases, however, it will be the considered judgment of elected representatives that controls, rather than the political and social preferences of a majority of unelected Commissioners.

III. CLARIFICATION OF THE FTC'S "UNFAIR OR DECEPTIVE ACTS OR PRACTICES" AUTHORITY

The second significant feature of the Chamber's legislative proposal concerns the FTC's exercise of its Section 5 "unfair or deceptive acts or practices" authority. In this connection, the Chamber carefully considered several alternative formulations that attempted to define prohibited acts and practices by specific category and type. However, as Congress itself concluded when it enacted the Wheeler-Lea amendments to the FTC Act, such an approach would be unworkable from any practical standpoint. As in the case of "unfair methods," the Chamber's proposed revision of the "acts and practices" language attempts to provide overall direction to the FTC and to define the limits of intervention in consumer protection matters.[18]

Under the current statutory formulation, the FTC's consumer protection jurisdiction extends to acts or practices that are "unfair or deceptive." Since this language was added to Section 5 in 1938, the Commission has made great strides in eliminating from the marketplace conduct that is "deceptive" in the traditional common law sense. Its premise has been that the free flow of accurate consumer information is essential to the competitive process and necessary for the efficient operation of markets—a premise that few would dispute. There is no arguing with the proposition, for example, that intentional or reckless misrepresentation of a product characteristic should be enjoined.

More recently, however, the FTC has gone significantly beyond traditional concepts of deception, all of which involve some element of improper motive or intent, in invoking its Section 5 "acts or practices" jurisdiction. The Commission has asserted authority under the "unfair or deceptive" rubric to reach conduct which, regardless of intent or motive, is merely alleged to have an adverse impact on consumers. In moving away from traditional deception to more subtle questions of consumer injury, the Commission is once again left without meaningful standards to guide its actions. All too often, the agency has used subjective perceptions of consumer impact as an excuse to embark upon experiments in social activism.

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[17] As the Commission itself recently observed, an agency "equipped with economic expertise" and "whose authority is limited to the issuance of prospective, nonpunitive orders to cease and desist" is especially able to adjudicate "sensitive issues" that may arise in more esoteric aspects of antitrust enforcement. Letter of Comm., per Chairman Miller, to Senators Packwood and Kasten dated March 5, 1982 at p. 5.

[18] The first minimal step with respect to the FTC's "unfair acts or practices" authority, of course, has been discussed earlier and concerns proposed legislation to make permanent the temporary provisions of Section 11(b) of the 1980 improvements Act which prohibit the FTC from initiating new magnuson-Moss rulemaking to regulate commercial advertising as an "unfair act or practice." Given the significant First Amendment considerations that exist in this area, "unfairness" is simply too vague a concept to be used in regulating advertising.

One recent example of the problems that can arise from the Commission's elastic application of its "unfair or deceptive" authority is the discredited, although technically still pending, product standards trade regulation rule.[19] The origins of this proceeding lie in legislation introduced in both the 94th and 95th Congresses by Senator Abourezk calling for federal regulation of the nation's product standards system. Although lengthy Senate hearings were held, the legislation remained stalled in Subcommittee, while a similar bill in the House did not even muster hearings. Despite this demonstrated absence of Congressional interest, the FTC took it upon itself to attempt to impose almost identical regulation of the standards process by a trade regulation rule.

The key issue raised by the standards proceeding is that our elected representatives, when presented with the opportunity, chose not to create laws in the area of voluntary standards setting. Nonetheless, the unelected FTC, insulated from responsibility to voters, has been trying to use its "unfairness" authority and the administrative process to accomplish the very same end.

Another controversial example of the FTC's expansive use of its "unfair or deceptive acts or practices" jurisdiction is the infamous children's advertising proceeding.[20] The Staff Report that recommended prohibition of televised advertising to young children offered three "justifications" for condemning such advertising as "unfair or deceptive," *i.e.*, (1) "the striking imbalance of sophistication and power" between advertisers and children; (2) the "manipulative—as opposed to informative—nature of the advertising"; and (3) the "unfairness of putting parents to a choice . . . between purchasing products advertised to children on television and enduring the conflict that goes with a refusal to buy the products." The first two of these "justifications," however, would apply to almost any advertising as the advertiser always possesses more "sophistication and power" than the average consumer and always hopes that his commercial message will "manipulate" the consumer, if that means inducing the consumer to make a purchase. As for the third "justification," the FTC's intrusion into parental supervision of children aptly earned the agency its pejorative nickname of "National Nanny." [21]

A third example of misguided "acts or practices" rulemaking is the FTC's proceeding against vocational schools.[22] This industry, which is composed of many honest small businessmen, had been criticized because of the sharp practices of a small number of school operators. Despite concerted efforts by both industry associations and state authorities to eliminate such abuse, the FTC nonetheless initiated a broad rulemaking designed to change the basic economics and business methods of the entire industry. In so doing, the Commission gave no consideration to the impact of its proposed action either on the many non-offending small businessmen or on the students themselves who, under the FTC's proposal, would have had to bear substantially increased tuition costs.[23] Had an appropriate cost-benefit analysis been undertaken, the vocational schools rulemaking would undoubtedly have had a significantly narrower and more appropriate focus.

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[19] The FTC announced its proposed trade regulation rule concerning standards and certification on December 7, 1978 (43 Fed. Reg. 57269). The new rule was to have become Part 457 of 16 CFR and would have made it both an "unfair method of competition" and "an unfair or deceptive act or practice" for any standards developer, certifier or marketer to violate its provisions. At the urging of the U.S. Chamber and other responsible business representatives, Congress enacted Section 7 of the FTC Improvements Act of 1980 prohibiting the Commission from promulgating a trade regulation rule concerning standards or certification activity under its Magnuson-Moss authority. Nonetheless, the Commission has kept the standards rulemaking alive under a different statutory provision of the FTC Act. See BNA Antitrust & Trade Reg. Rep., No. 987 at A-19 (October 30, 1980).

[20] The FTC published a formal announcement on April 27, 1978 initiating a trade regulation rule proceeding to deal comprehensively with the entire area of television advertising to children (43 Fed. Reg 17967). The Congress quite properly terminated this exercise as inappropriate social engineering when it adopted Section 11 of the 1980 Improvements Act prohibiting promulgation of any rule with respect to such advertising under the Commission's "unfair acts or practices" jurisdiction.

[21] Another example of the FTC's overzealous efforts to regulate the field of commercial advertising under its expansive notions of "unfairness" and "deception" is the "Proposed Rule Concerning Advertising for Over-the-Counter Drugs," announced November 11, 1975 (40 Fed. Reg. 52631). Under this proposal, all advertising for OTC drug products would have been limited strictly to labeling language approved by FDA, thus turning television commercials for such products into a dry recitation of ingredients, warnings, etc. The Commission properly terminated this unwise effort, after several years of costly proceedings, on May 1, 1981 (46 Fed. Reg. 24584).

[22] The FTC issued its "Proprietary Vocational and Home Study Schools" trade regulation rule as Part 438 of 16 CFR on December 28, 1979 (44 Fed. Reg. 32207). The rule, however, was subsequently overturned by the court of appeals in *Katherine Gibbs School* v. *FTC*, 612 F.2d 658 (2d Cir. 1980).

The Commission itself has recognized the problems inherent in its undefined "unfair or deceptive acts or practices" authority when used outside the area of traditional deception and has, on several occasions, issued policy statements attempting to clarify the issue.[24] In December of 1980, for example, the Commission submitted to the Consumer Subcommittee a lengthy "Statement of Policy" concerning the scope of its consumer unfairness jurisdiction.[25] The Commission expressly reaffirmed that Policy Statement in its most recent March 5, 1982 letter to this Committee and has further suggested that formal codification of the principles articulated in the Statement would be appropriate at this time.[26]

In both its March 5 letter and the December 1980 Policy Statement, the Commission identified the concept of "consumer injury" as the primary focus of the agency's authority to prohibit non-deceptive trade practices on "unfairness" grounds. At the same time, the Commission acknowledged that the consumer injury is legally "unfair." Rather, to justify a finding of unfairness, the injury must also satisfy the following three tests:

1. The anticipated injury must be substantial and involve economic or monetary harm, rather than subjective harms such as emotional distress or offenses to taste or social belief;
2. The injury must not be outweighed by any countervailing benefits to consumers or competition that the practice produces; and
3. It must be an injury that consumers themselves could not reasonably have avoided.

The U.S. Chamber's legislative proposal simply takes the Commission at its word and defines unfair or deceptive acts or practices under Section 5 to be those which: "directly cause or may foreseeably result in substantial economic injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition. . . ."

The Chamber's proposal would not impair the FTC's current authority to condemn and prevent actual "deception." Falsehoods and intentionally misleading representations have no proper place in a well-functioning free market. By its very nature, such fraudulent behavior is intended to inflict and does inflict substantial injury on consumers. Because such conduct has no redeeming virtue and cannot be reasonably avoided, FTC enforcement action against acts and practices that have been traditionally recognized as "deceptive" can, under the Chamber's proposed legislation, continue as in the past.

With respect to the more elusive category of acts and practices which are alleged to be "unfair or deceptive" based solely on claims of adverse consumer impact, however, the Chamber's proposed amendment codifies the FTC's most recent pronouncements that "substantial" injury is an essential element of such a violation. It insures that the FTC's limited enforcement resources will be spent on matters of real economic signficance, and not wasted on non-existent, trivial or merely speculative harms.

The Chamber's proposal also incorporates the concepts of "reasonable avoidability," as well as a basic cost-benefit analysis, as part of the broader assessment of consumer impact. Each of these factors was expressly identified by the Commission in its most recent letter to this Committee as an appropriate predicate to the exercise of its "acts or practices" authority over "unfair" conduct.[27] By incorporating these elements in the organic statute along with the fundamental "substantial injury" test, both the public and reviewing courts can be sure that the key criteria articulated by the Commission will be given the force of law and cannot be ignored by the agency in the future.

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[23] *See* Ellis, "Legislative Powers: FTC Rulemaking in The Federal Trade Commission Since 1970" at 177 (Clarkson & Muris ed. 1981).

[24] See, e.g., Statement of Basis and Purpose of Trade Regulation Rule 408, Unfair or Deceptive Advertising and Labeling of Cigaretts in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8355 (1964).

[25] Letter of Comm., per Carol M. Thomas, Secretary, to Sen. Wendell H. Ford and Sen. John C. Danforth dated December 17, 1980.

[26] Letter of Comm., per Chairman Miller, to Senators Packwood and Kasten dated March 5, 1982.

[27] While the Commission's March 5 letter suggests that a highly quantitative cost-benefit analysis may not be appropriate in every case, the analysis should at least "take into account costs related to a prospective remedy, including but not limited to direct cost to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and captial formation and like matters." (*Id.* at p. 8.)

IV. ELIMINATION OF OVERLAPPING REGULATORY JURISIDICTION

The third and final element of the Chamber's proposed legislation deals with the FTC's increasingly vexations use of its Section 5 "acts or practices" authority as a backstop for the perceived deficient performance of other agencies or, in some cases, even of Congress. Rather than focusing its energies on the commercial sales and marketing issues which are its special province, the FTC has attempted to extend its consumer protection jurisdiction to issues such as product design, safety and environmental effect which generally fall within the appropriate competence of other specialized regulatory bodies. In other instances, even though Congress may have determined not to act with respect to a particular area, the FTC has been all too willing to intervene and impose its own regulation under color of the Section 5 "acts or practices" authority.

In certain respects the children's advertising proceeding contained a strong undercurrent of this sort of Commission attitude. To the extent the proceeding focused on sugared food products, the attack was motivated not so much by any concern for deceptive or misleading advertising, but rather by the unarticulated notion that sugared foods are simply bad for children. Because even the Commission recognized that it had no power to banish such products from the grocery shelf by administrative fiat, it nonetheless tried to do the next best thing by prohibiting manufacturers from advertising the products' existence. While the FTC may properly control abusive marketing practices, it should not be in the business of determining whether a product is fundamentally good or bad and thereby usurp consumer choice.

Similarly, the Commission has initiated a number of proceedings which, although technically cast in terms of advertising and marketing practices, actually turn on issues of basic product design. Thus, the agency is currently engaged in litigating the safety of tractor gas tanks [28] and has recently obtained a consent order that requires warning stickers on new jeep vehicles advising of potential handling and driver control problems.[29]

In other instances, the FTC has stepped in despite Congress' judgment that a particular type of regulation is either unwise or unnecessary. In the Fair Debt Collection Practices Act (15 U.S.C. § 1682 *et seq.*), for example, Congress expressly exempted attorneys and certain retailers from coverage of the statute. Despite this explicit statement of Congressional intent, the FTC has used its Section 5 "acts or practices" authority to extract consent orders from exempted individuals and businesses which essentially duplicate the statutory requirements. Such overreaching by the Commission is particularly inappropriate in this case, where Congress has already provided a mechanism in the statute for yearly reports and recommendations from the agency to permit legislative modification when and if necessary. Under Section 5, however, the Commission was able to short-circuit this process and effectively "legislate" its own ad hoc repeal of the statutory exemptions.

The Chamber believes that Congress never intended to make the Commission an all purpose consumer protection agency. Congress has established specialized regulatory bodies with appropriate competence, such as the National Highway Traffic Safety Administration, the Consumer Product Safety Commission, and the Environmental Protection Agency, to deal with complex product design, safety and environmental problems. Therefore, it is inappropriate for the Commission, acting in the name of consumer protection, to invade areas which Congress has determined either to exempt or else to commit to the specific jurisdiction of one of the more specialized regulatory authorities.

The Chamber's proposed legislation would help to alleviate this problem by prohibiting FTC exercise of its Section 5 "acts or practices" powers with respect to conduct that is authorized by federal statute or subject to the direct regulatory authority of another federal agency. In this way, the proposal would eliminate possible jurisdictional conflicts and prevent Commission interference in matters best left to the expertise of Congressionally-established specialized agencies. Perhaps most important, it would also give the Commission clear direction to focus its energies on traditional marketing issues, rather than try to play the role of universal consumer protector.

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[28] *International Harvester*, FTC Docket 9147, concerning "fuel geysering" problem of farm tractors.

[29] *American Motors Corp.*, 3 CCH Trade Reg. Rep. ¶ 21,890, consent order to cease and desist announced November 10, 1981.

V. REPEAL OF SECTION 5(m) (1) (B)

Finally, in addition to its affirmative legislative proposals, the U.S. Chamber also urges that Section 5(m)(1)(B) of the Federal Trade Commission Act be repealed.

Under Section 5(m)(1)(B), the FTC is able to seek civil penalties of up to $10,000 per violation from companies for violating final cease and desist orders entered in proceedings against other firms. Section 5(m)(1)(B) does not require that the company from which the FTC is seeking penalties was actually a party to, or had prior notice of and an opportunity to be heard in, the original cease and desist proceeding. Instead, all that is required is that the charged company (1) engage in an act or practice after a cease and desist order with respect to such act or practice has become final and (2) have "actual knowledge" by virtue of that cease and desist order that the act or practice in question has been found "unlawful." In effect, Section 5(m)(1)(B) turns cease and desist orders into general rules without even the minimal due process protections applicable to agency rulemaking under the Administrative Procedure Act.

When originally enacted in 1975, Section 5(m)(1)(B) was intended to enable the FTC, after it had fully and fairly litigated the lawfulness of a particular act or practice against one respondent, to move quickly and effectively against other firms using the same practice in the same or similar circumstances. Experience with the FTC's exercise of its new Section 5(m)(1)(B) authority since that time clearly demonstrates that, however reasonable that intent of Congress may have been, the procedure is inherently unfair and subject to manipulation and abuse.

Thus, rather than employ its Section 5(m)(1)(B) powers as a means of follow-up enforcement to properly litigated proceedings, the FTC has undertaken a program of wholesale mailings of both old and new orders, including many of an extremely general nature and application. It has done so despite the plain prospective wording of the statutory language which contemplates that only Commission determinations made after January 1975 are to be used as a basis for bringing a penalty action.[30] By this device, the agency is in a position to eschew conventional proceedings and to claim, on the basis of ancient orders, penalties of $10,000 per violation against companies on its mailing list.

The FTC's 1978 "down products" mailing illustrates how Section 5(m)(1)(B) has been misused. In that case, the Commission sent out to 250 industry members a "notice package" containing orders dealing with the labeling of down products made between 1942 and 1957—although an important Seventh Circuit reversal of a highly relevant Commission decision in this area was omitted. In addition, the Commission's Staff Enforcement Policy Statement, which was included in the notice package, declared that failure to comply with the Commission's 1971 *Down Products Guides* would be deemed to be a violation of the 1942-1957 orders despite the fact that: (1) the labeling standards contained in the 1971 *Guides* were substantially different from those in the 1942-1957 determinations; (2) no cases had been brought since the 1971 *Guides* were adopted; and (3) the FTC had previously stated that the *Guides* have no force of law or precedential value, are only advisory in nature and merely represent the Commission's opinion as to what might be an unfair or deceptive practice. Clearly, this sort of informal rulemaking by the Commission's staff, without hearings or other procedural safeguards, was never intended under Section 5(m)(1)(B).

Furthermore, the Section 5(m)(1)(B) authority also creates a distinct potential for manipulation of the administrative process even when an actual cease and desist hearing is held. For example, the FTC can select as a respondent the firm which, for financial or other reasons, is least able to mount an effective defense. Thereafter, the agency can seek to use any final cease and desist order entered against such a respondent, whether or not tested on judicial review, as a conclusive determination of the legality of the practice in civil penalty proceedings against other companies.[31] Indeed, although the FTC asserts that it will only use its Section 5(m)(1)(B) authority with respect to litigated cease and desist cases, there is nothing in the statute itself which would prevent the bringing of a civil penalties proceeding based on a negotiated consent order.

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[30] Section 5(m)(1)(B) provides in pertinent part: If the Commission *determines* in a proceeding under subsection (b) . . . and *issues* a final cease and desist order with respect to such act or practice, the Commission may commence a civil action to obtain a civil penalty in a district court . . . Under the plain meaning of the underscored words in the present tense, Congress intended that the provision be applied prospectively only, *i.e.*, on the basis of legal principles established in determinations (final orders) made after the January 4, 1975 effective date of the statute.

[31] Under Section 5(m)(2), only "issues of fact" are open for litigation in the civil penalties action by a defendant which was not specifically named in the original cease and desist order.

The only judicial authority interpreting Section 5(m)(1)(B), an interlocutory district court decision,[32] has created a great deal of confusion. Acknowledging the obvious due process problems inherent in this provision, the district court held that a civil penalties defendant was certainly entitled to litigate both whether it had "actual knowledge" of the "unlawfulness" of its conduct and whether its conduct was different from that proscribed in the earlier order. In addition, the court further suggested that, "in an appropriate case," a defendant might defend on grounds of lapse of time and changed conditions, or perhaps even attack the legal sufficiency under Section 5 of the FTC's prior determination. Thus, the court's decision has created substantial uncertainty as to exactly what is open for litigation in a Section 5(m)(1)(B) penalty proceeding.

The fundamental defect of Section 5(m)(1)(B) is its failure to safeguard one's right not to be held liable for civil penalties without a reasonable opportunity to establish the legality of one's conduct. Because there is no requirement in the statute for prior notice and an opportunity to be heard, the FTC can demand enormous monetary penalties on the basis of old orders or, alternatively, by picking on the weakest target and extending a resulting cease and desist order industrywide. Basic fairness and due process require that the FTC be prepared to litigate the legality issue fully and fairly against all industry members that may be affected before civil penalties can be imposed.

In addition, Section 5(m)(1)(B) suffers from vague and ambiguous drafting. Although the entire provision is premised upon the existence of a final cease and desist order, a defendant may be held liable for civil penalties based upon "actual knowledge that [an] act or practice is unfair or deceptive," irrespective of actual knowledge of the prior order. Similarly, because statutory liability arises merely from a "final" order, rather than one entered after hearing and decision, there is a danger that Section 5(m)(1)(B) civil penalties could be sought on the basis of a negotiated consent order without any adversarial testing of legality.

All of these problems are further compounded by the possibility that $10,000 penalties may be imposed for "each violation" (emphasis added). What constitutes an individual violation, however, is nowhere defined, nor is any maximum number of possible violations resulting from a single transaction specified. As recent cases demonstrate, one bulk mailing or the circulation of single publication may result in millions of separate violations and potential civil penalties measured in billions of dollars.[33]

For all these reasons, the U.S. Chamber believes that the only sensible solution to the Section 5(m)(1)(B) problem is repeal of the provision *in toto.*

CONCLUSION

The Chamber appreciates the opportunity to bring the views of its members to the Subcommittee's attention. We are confident that these important issues will be debated fully and fairly, and we hope that the concepts incorporated in our proposals will provide a basis for constructive legislative supervision of the Commission's future activities.

APPENDIX—DRAFT LEGISLATION TO CLARIFY FTC'S POWER TO PREVENT "UNFAIR METHODS OF COMPETITION" AND "UNFAIR OR DECEPTIVE ACTS OR PRACTICES"

I. Amend Section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. § 45(a)(1)) to read as follows: "(1)(A) Unfair methods of competition in or affecting commerce are declared unlawful: *Provided, however,* That no method of competition shall be deemed to be unfair unless it—(i) violates sections 1 or 2 of the Sherman Act; or (ii) is expressly defined to be an unfair method of competition by Federal statute.

(B) Unfair or deceptive acts or practices in or affecting commerce, where such acts or practices directly cause or may foreseeably result in substantial economic injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition, are declared unlawful."

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[32] *United States* v. *Braswell, Inc.*, 1981-2 Trade Cases ¶ 64,325 (N.D. Ga. 1981).

[33] *E.g., United States* v. *Golden Fifty Pharmaceutical Co., Inc.*, 421 F. Supp. 1199 (N.D. Ill. 1976) (ruling that government could have charged 25 million violations, one for each copy of a comic book containing an offending advertisement); *United States* v. *Reader's Digest Ass'n, Inc.*, 662 F.2d 955 (3d Cir. 1981), *cert. denied,* 50 L.W. 3570 (1982) (bulk mailing of 16 million copies of an advertisement constituted as many separate violations).

II. Amend Section 5(a) of the Federal Trade Commission Act (15 U.S.C. §45(a)) by adding a new paragraph (3) which reads: "(3) Nothing in subparagraph (1)(B) of this subsection shall apply to any act or practice which is authorized by Federal statute or subject to the direct regulatory authority of another Federal agency."

III. Repeal Section 5(m)(1)(B) of the Federal Trade Commission Act (15 U.S.C. §45(m)(1)(B)).

Senator **Kasten**. Mr. John Montgomery, Chief, Consumer Protection Division, Department of the Attorney General of Massachusetts.

Mr. Montgomery.

Mr. **Montgomery**. Thank you, Mr. Chairman, members of the committee. I want to thank you for the opportunity to discuss the array of proposals which have surfaced in recent weeks to alter the scope of the proscription in the Federal Trade Commission Act against unfair and deceptive practices. We are very concerned that a number of these proposals, if adopted, would reverse 44 years of sound law developed by the Commission and the Federal courts to protect consumers.

Of particular importance, from our perspective in the States, is that we believe enforcement of State consumer protection laws in all 50 States may be dramatically altered by a reversal of longstanding Federal policy in this area. Our statutes stem from a strong legislative recognition that strict common law notions of fraud developed in a simpler economic world do not work in the complexities of the modern marketplace. The proposals being considered by the committee, if adopted, run the risk of resurrecting caveat emptor from the realm of historical curiosity to haunt the modern marketplace.

I want to briefly run through the history of the recent development of State statutes to protect consumers, and I have done this in much more detail in my written statement. Since the late 1960's, all 50 States have enacted legislation which is modeled after the Federal Trade Commission Act. These statutes had their genesis in various models suggested by the FTC itself; virtually every State prohibits deceptive practices, while approximately 30 States also prohibit unfair acts or practices. The State statutes are enforced almost exclusively through recourse to State judicial systems by State attorneys general, and in 42 States by consumers through private civil actions.

State courts have embraced these acts as a flexible, practical and effective approach to many marketplace abuses. Literally hundreds of appellant decisions in the various States have interpreted and applied these statutes in recent years to consumer claims in a variety of contexts. The States have unhesitatingly adopted the defintions of unfairness, and in particular, deception, which had been formulated by the Federal Trade Commission and the Federal courts through the years.

In fact, more than 20 statutes declare that State courts shall be guided by interpretations given by the Federal Trade Commission and the Federal courts to section 5(a) of the act. Even where statutes do not direct that State courts shall follow the Federal Trade Commission, most State courts have interpreted their State acts consistently with interpretations of the Federal act because of similarity in language and purpose between the statutes.

Frankly, I am not aware of any substantial criticism in the States, either from business groups or in legal or trade publications of the prevailing standards for unfair or deceptive practices as applied to individual adjudications. Needless to say, we are opposed to fixing a system which does not appear to be broken.

Now, a number of proposals have been advanced to limit the phrase "unfair or deceptive" and I want to make a brief comment just on two of them. First, with respect to the proposal to limit unfair or deceptive acts or practices by a so-called cost-benefit analysis, we agree that that approach has some historical applicability to the word "unfair" but we do not think it has any basis in the law of deception, and in our opinion its adoption would render the proscription against deceptive practices unenforceable in most State or Federal cases.

The cost-benefit proposal apparently alters the burden of proof necessary to establish that a practice is deceptive. In my view, it opens new vistas for litigation over the proper definition of substantial injury or benefit, and the quantum of proof and acceptable methodologies for establishing values for those terms. We agree the cost-benefit analysis has a place; it is a useful administrative policymaking tool, and can assist us in making informed judgments as to which cases we choose to prosecute. But that is where it should stay. It has no place, in our view, in a legislative standard. We think that the FTC really has admitted as much in Chairman Miller's March 5 letter to the committee in which he draws a very careful distinction between qualitative and quantitative cost-benefit analysis. I am puzzled as to how the Congress might reduce a qualitative judgment to a coherent legislative standard.

Chairman Miller also suggested that Congress define deception to reach only acts or practices which are likely to deceive reasonable consumers rather than the existing standard which applies to practices which have the capacity or tendency to deceive consumers. In the case of particularly vulnerable consumers he would impose liability only if the business knew or should have known of the likelihood of deception.

This attempt by the Chairman to limit the protections of deceptive trade practices law to only a limited class of consumers will not work in the real world of State and Federal law enforcement. The FTC and State attorneys general apply the law to practices affecting large classes of consumers, and this suggested change would require prosecutors to prove the reasonableness of consumer conduct, and predictably, I think it would require years of case-by-case adjudication to define the standards of reasonableness as well as acceptable methodologies of proof.

These proposals are designed to substantially reduce the standards of acceptable business conduct under the law. If these proposals are adopted, so-called vulnerable consumers—the elderly, also the sick, the handicapped and other regular targets of deceptive practices—will suffer the economic losses in the face of the defense of good faith or lack of intent or lack of knowledge.

Mr. Chairman, I think that we have been down that road before. Under the common law, neither consumers nor business were satisfied with the result. Thank you.

[The statement follows:]

STATEMENT OF JOHN T. MONTGOMERY

Mr. Chairman and Members of the Committee: My name is John T. Montgomery. I am an Assistant Attorney General and Chief of the Consumer Protection Division of the Department of the Attorney General for the Commonwealth of Massachusetts. I am here today representing Attorney General Francis X. Bellotti, who serve as Chairman of the Consumer Protection Subcommitteee of the National Association of Attorneys General.

Thank you for the opportunity to discuss the array of proposals which have surfaced in recent weeks to alter the scope of the proscription against "unfair or deceptive acts or practices" in ¶5(a) of the Federal Trade Commission Act. We believe that a number of these proposed amendments, if adopted, would reverse 44 years of jurisprudence developed by the Federal Trade Commission (FTC) and the Federal Courts to protect consumers against marketplace abuses. In addition, the enforcement of state consumer protection laws in all 50 states may be dramatically altered by a reversal in longstanding federal policy in this area.

These state laws were not enacted to place unwarranted burdens on honest business people. They stem from a strong legislative recognition that strict common law notions of fraud developed in a simpler economic world do not work in the complexities of the modern marketplace where consumers are often in unequal bargaining positions with sophisticated businesspeople. As I will explain, adoption of the various proposals before the Committee will gut the principles of existing consumer protection law. These proposals run the risk of resurrecting the rule of caveat emptor from the realm of historical curiousity to haunt the modern marketplace.

I. SYNOPSIS OF STATE MINI-FTC ACTS

At the outset, I want to briefly review the history of the recent development of state statutes to protect consumers from unfair or deceptive practices. Since the late 1960's, all 50 states have enacted consumer protection legislation which parallel the FTC Act. See Exhibit A for a compilation of state statutes. These statutes had their genesis in various models suggested the FTC and the Commissioners on Uniform State Laws, and were designed to "create a more equitable balance in the relationship between consumers and business".

Virtually every State prohibits deceptive practices, while approximately 30 States also prohibit unfair acts or practices. In contrast to the FTC Act, these state statutes are enforced almost exclusively through recourse to state judicial systems, rather states empower the Attorney General to enforce the statutory standards, and to obtain injunctive and monetary relief on behalf of residents of the state through the state courts. In addition, forty-two state statutes expressly provide that consumers may bring civil actions for damages and other relief in state courts. The statutes generally provide that a prevailing consumer is entitled to attorneys fees. The fee award provisions are designed to encourage consumers to enforce state statutes by ensuring that competent counsel will be available to represent them.

State courts have embraced the state consumer protection acts as a flexible, practical, and effective approach to many marketplace abuses, consistently recognizing that they represent a needed change from the traditional common law approaches to consumer redress. *E.g., Perlman* v. *Time, Inc.*, 64 Ill. App. 3d 190, 380 N.E.2d 1040 (App. Ct. 1978); *Slaney* v. *Westwood Auto, Inc.*, 366 Mass. 688, 322 N.E.2d 768 (1975); *Kulger* v. *Romain*, 58 N.J. 522, 279 A. 2d 640 (1971). Despite the relatively slow evolution that is characteristic of most new statutes, literally hundreds of appellate decisions in the various states have interpreted and applied these statutes to consumer claims in a variety of contexts, including advertising, *e.g., Dollar-A-Day Rent-A-Car Systems* v. *Mountain States Telephone and Telegraph Co.*, 22 Ariz. App. 270, 526 P.2d 1068 (1974); *People* v. *Lynam*, 253 Cal. App. 2d 959, 61 Cal. Rptr. 800 (1967); *Williams* v. *Bruno Appliance and Furniture*, 62 Ill. app.3d 219, 379 N.E.2d 52 (App. Ct. 1978); *Hockley* v. *Hargitt*, 82 Wash. 2d 337, 510 p.2d 1123 (1973); automobile repairs, *e.g., Witters* v. *Daniels Motors, Inc.*, 524 P.2d 632 (Colo. Ct. App. 1974); *State* v. *Aamco Automatic Transmissions, Inc.*, 293 minn. 342, 109 N.W.2d 444 (1972); *Doyle* v. *Grady*, 543 S.W.2d 893 (Tex. Civ. App. 1976); *State* v. *Ralph Williams' North West Chrysler Plymouth, Inc.*, 87 Wash. 2d 298, 553 P. 2d 423 (1976); employment opportunities, *e.g., Searle* v. *Exley Express, Inc.*, 278 ore. 535, 564 p.2d 1054 (1977); banking and credit, *e.g.*, *Garland* v. *Moble Oil Corp.*, 340 F. Supp. 1095 (N.D. Ill. 1972) *Chern* v. *Bank of America*, 15 Cal. 3d 866, 544 p.2d 1310 (1976); debt collection e.g., *Schubach* v. *Household Finance Corp.*, 376 N.E.2d 140 (Mass. 1978); *State* v. *Credit Bureau of Laredo*, 530 S.W.2d 288 (Tex. 1975); funeral practices, *e.g.*, *State* v. *Limbrecht*, 246 N.W.2d 330 (Iowa 1976); *Olwe* v. *Graceland Sales Corp.*, 61 N.J. 182, 293 A.2d 658 (1972); home improvement, *e.g.*, *Perma Stone Corp.* v. *Merkel*, 255 Wis. 565, 39 N.W.2d 730 (1949), *Hulbert* v. *Cottier*, 56 Ill. app. 3d 893, 372 N.E.2d 734 (App. Ct. 1974); insurance, *e.g.*, *Ray* v. *United Family Life Ins. Co.*, 430 F. Supp. 135 (W.D. N.C. 1977), *Dodd* v. *Commercial Union Insurance Co.*, 365 N.E.2d 802 (Mass. 1977); landlord-tenant, *e.g.*, *York* v. *Sullivan*, 369 Mass. 125, 388 N.E.2d 341 (1975), *Commonwealth* v. *Minumental Properties, Inc.*, 459 Pa. 450, 329 A.2d 812 (1974); medical devices, *e.g.*, *Hearing Aid Association* v. *Bulluck*, 413 F. Supp. 1032 (E.D. Ky 1976); pyramid sales, *e.g.*, *People* v. *Bestline Products, Inc.*, 61 Cal. App. 3d 879 132 Cal. Rpt. 767 (Ct. App. 1976); *State* v. *Dare To Be Great, Inc.*, 15 N.C. 275, 189 S.E.2d 802 (Ct. App. 1972); real estate, *e.g.*, *Young* v. *Joyce*, 351 A.2d 857 (Del. 1975); *Nash* v. *Hoopes*, 332 A.2d 411 (Del. Super. Ct. 1975); *Heller* v. *Silverbranch Constr. Co.*, 382 N.E.2d 1065 (Mass. 1978); and breach of warranty, *e.g.*, *People* v. *Conway*, 42 Col. App. 3d 875, 117 Cal. Rptr. 251 (1974); *Attway* v. *Tom's Auto Sales, Inc.*, 144 Ga. App. 813, 242 S.E.2d 742 (Ct. App. 1978); *Volkswagen of America, Inc.* v. *Licht*, 544 S.W. 2d 442 (Tex. Civ. App. 1976); *Slaney* v. *Westwood Auto, Inc.*, *supra.*

Following the FTC model, these state acts do not provide any strict definition of "unfair or deceptive". This, of course, is because the nearly limitless forms in which a business can act to cause consumer harm do not lend themselves to precise definition. To the extent any definition of "unfair or deceptive" is provided, it gives the opportunity to a crafty businessperson to get around that definition. Congress and state legislatures recognized this, and so they purposely refused to limit "unfair or deceptive" by trying to define those terms exactly.

The unhesitating adoption of expansive definitions of "unfairness" and "deception" by state courts has depended heavily on the wealth of jurisprudence in the area developed by the FTC and the federal courts. In fact, more than twenty state statutes declare that "it is the intent of the legislature that in construing . . . this act the courts will be guided by the interpretations given by the Federal Trade Commission and the Federal Courts to Section 5(a)(1) of the Federal Trade Commission Act".[1] Moreover, even where the statutes do not contain this specific directive, most state courts have interpreted their state acts consistently with § 5(a) of the FTC Act because of the similarity in language and purpose between the federal and state statutes.[2]

A. DECEPTION

The law of deception under these state acts has been interpreted broadly. The state courts, consistent with interpretations of § 5(a) have construed their statutes as designed to protect "ignorant and unthinking" consumers, and have found an act to be deceptive if it has the capacity or tendency to deceive. *E.g.*, *Chern* v. *Bank of America*, 15 Cal. 3d 866, 127 Cal Rptr. 110, 544 P. 2d 1310 (1976); *People ex. rel.* v. *Lefkowitz* v. *Volkswagen of America, Inc.*, *47 App. Div.* 2d 868, N.Y.S. 2d 157 (App. Div. 1975); *Spradling* v. *Williams*, 553 S.W. 2d 143 (Tex. Civ. App. 1977; *State* v. *Packard*, Clearinghouse No. 27, 066 (Vt. Super. Ct. 1977); *State* v. *Ralph Williams' North West Chrysler Plymouth, Inc.*, 87 Wash. 2d 298, 553 P. 2d 423 (1976). The focus of the law of deception is on the effect of an act or practice on the consumer. As the Massachusetts Supreme Judicial Court has noted, a practice is deceptive if it "could reasonably be found to have caused the consumer to act differently from the way he

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[1] This or similar language is found in the following statutes: Alaska Stat. § 45.50.545, Ariz. Rev. State. § 44-1522(B), Conn. Gen. State. Ann. § 42-110(B), Fla. Stat. Ann. § 501.204, Ga. Code Ann. § 106-1201, Haw. Rev. Stat. § 408-3, Idaho Code § 48-604, Me. Rev. Stat. tit. 5 § 207(1), Md. Com. Law Code Ann. § 13-105, Mass. Gen. laws Ann. c.93A § 2(b), Mont. Rev. Codes Ann. § 85-403, NH Rev. Stat. Ann. § 358-A-13, NM Stat. Ann. § 49-15-4, RI Gen. Laws § 6-13.1-3, SC Code § 66-71.1, Tenn. Code Ann § 47-18-115, Utah Code Ann. § 13-11-4, Vt. Stat. Ann. tit. 9 § 2453, W. Va. Codes § 46A-6-103.

[2] See, *e.g.*, *People ex rel. Dunbar* v. *Gym of America, Inc.*, 177 Colo. 97, 493 p.2d 660, Pov. L. Rep. ¶ 15,517 (1972); *Fitzgerald* v. *Chicago Title and Trust Co.*, 46 Ill. App. 3d 526, 5 Ill. Dec. 94, 361 N.E.2d 94 (1977); *Gour* v. *Daray Motors*, 373 So.2d 571 (La. App. 1979); *State ex rel. Guste* v. *Alaska Overseas, Inc.*, Clearinghouse No. 26,208 (La. Ct. of App. 1977); *People ex rel. Lefkowitz* v. *Colorado State Christian College*, 76 Misc. 2d 50, 346 N.Y.S. 2d 482 (Sup Ct. 1973); *Hardy* v. *Toler*, 288 N.C. 303, 218 S.E.2d 342 (1975); *Thomas* v. *Sun Furniture and Appliance Co.*, 11 Ohio Op. 3d 26 (CT. App. 1978) *Americans Be independent* v. *Commonwealth*, 14 Pa. Commw Ct. 179, 321 A.2d 721 (1974); *State* v. *Credit Bureau of Laredo*, 530 S.W.2d 288 (Tex. 1975); *Lightfoot v. MacDonald*, 86 Wash. 2d 331, 544 p. 2d 88 (1976).

otherwise would have acted". *Lowell Gas Co.* v. *Attorney General, 377 Mass. 37 (1979), 385 N.E. 2d 240 (1979). Because the law of deception is committed to insuring a marketplace where consumers need not be wary of hidden deceptions, state courts, like the FTC, do not require that consumers prove intent to deceive, or knowledge of the deception on the part of the business. See, e.g., Testo* v. *Russ Dunmire Oldsmobile,* 16 Wash. App. 39, 554 P. 2d 349 (1976); Bull v. *Kent-Brown Chevrolet,* 1 Kan. App. 131, 561, P. 2d 907 (Ct. App. 1977), *Slaney* v. *Westwood Auto, Inc.*, 366 Mass. 688, 322 N.E. 2d 768 (1975).[3] Thus, the business community is subject to a uniform requirement imposed on all market participants to consider the effect of marketing practices on all segments of the buying public. State courts have uniformly recognized that this approach, developed over the years under the FTC Act, is essential to consistent, uniform, and fair application of law.

B. UNFAIRNESS

As might be expected, the law of "unfairness" has not been applied as extensively as the "deception" standard in the states. Given the broad nature of the term "unfair" and the lack of specific common law roots for the concept, it would not be surprising if the state court judges were disinclined to apply the standard at all. To the contrary, however, state courts have relied on the experience of the FTC, and held that standards enunciated in the Cigarette Rule by the FTC and approved by the Supreme Court in *Sperry & Hutchinson Co.* v. *FTC* provide an adequate basis by which unfairness may be applied through "the gradual process of inclusion and exclusion" by the judiciary. Despite the expansive nature of unfairness, state court decisions generally exhibit a relatively commonplace application of the term. For example, state courts decisions have established that it is unfair for a seller to breach a product warranty, *e.g., People* v. *Conway, supra,* to charge unconscionable prices, *e.g., Commonwealth* v. *DeCotis,* 366 Mass. 234, 316 N.E. 2d 748 (1974), or to use high pressure sales tactics, *Commonwealth* v. *Handicapped Industries, Inc.*, Clearinghouse No. 26,027 (Pa. C.P. 1977), or for a landlord to fail to maintain leased premises in a habitable condition, *e.g., Wolfberg* v. *Hunter,* 385 Mass. 390 (1982), or for creditors or collection agencies to engage in abusive collection practices, *Barquis* v. *Merchants Collection Assn., 7 Cal. 3d 94, 101 Cal. Rptr. 745 (1972).*

State courts, then, have interpreted both deception and unfairness broadly to equalize the bargaining positions of consumers and businesses. These expansive interpretations have strong roots in the common law, but also result from legislative intent to move the common law forward into the complexities of the modern day marketplace. It is primarily because "unfair" and "deceptive" have not been defined precisely in state statutes that the state laws have been so successful in dealing with the myriad of harmful business activities that have sprung up in recent years.

II. PROPOSALS TO AMEND SECTION 5(a) OF THE FTC ACT

A number of proposals have been advanced to limit the phrase "unfair or deceptive" by: (1) introducing cost-benefit considerations to the determination of liability; (2) requiring actual consumer injury as a result of a deceptive practice; (3) limiting deception to representations of fact rather then opinion; (4) and restricting the protections of the law of deception to reasonable consumers, rather than the "ignorant, unthinking" consumer.

As a preliminary matter concerning these proposals, the Committee should realize that it is being asked to choose between two very different legal standards for consumer protection law. As discussed above, a body of law already exists in the form of FTC decision and hundreds of state court appelate decisions all defining unfair or deceptive trade practices. If section 5(a) is amended as proposed, this body of law will disappear on the federal level and will be seriously jeopardized in the state courts. The proposals to this Committee do not create a new body of law to take its place. Rather, a new set of undefined and general legislative instructions will be the replacement. While these new instructions clearly reflect a particular political and economic ideology, terms such as "benefits", "costs" and "reasonableness" are nevertheless merely general instructions. In our view, consumer protection is simply not an area that lends itself to a very precise statutory standard. Moreover, general political and economic theories as expressed in this proposed statute have limited value in the context of case-by-case litigation. As a result, both consumers and business will be subject to greater uncertainty than under present law.

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[3] The elements of deception differ substantially from the common law of fraud or deceit, which traditionally requires proof of intent to defraud, and knowledge of falsity of a representation. However, it is import to note that the law of deception is consistent with emerging common law trends recognizing the tort of innocent or negligent misrepresentation, which do not necessarily require proof of knowlege or intent. See, Prosser, Law of Torts, at 710.

A. COST-BENEFIT ANALYSIS

It has been proposed in S. 1984 that the phrase "unfair or deceptive" be limited to acts or practices which "cause substantial consumer injury that outweighs benefits derived from the act". This cost-benefit approach, as the Committee knows, was outlined by the FTC in December, 1980 as a proper interpretation of case law limiting the authority of the Commission to proscribe unfair trade practices. This concept, however, has no historical basis in the law of deception and in our opinion its adoption would render the proscription against deception unenforceable in most federal or state cases.

It is our understanding that the primary purpose of this proposal is to overrule current law that defines a practice as deceptive if it has the capacity or tendency to deceive, without proof of actual deception. This important principle is, of course, thoroughly imbedded in both state and federal law, and for good reason. The "capacity or tendency" standard establishes a burden of proof that can be applied consistently to complex cases involving thousands of consumers. In addition, at the state level, it permits attorneys general to seek temporary injunctive relief to halt serious deceptive practices, particularly by marginal or fly-by-night companies, before substantial harm to public has occurred, and without the necessity of proving the extent of the actual resulting injury.

The cost-benefit proposal alters burden of proof necessary to establish that an act or practice is deceptive. In addition, it opens new vistas for litigation over the proper definition of "substantial injury" or "benefit", and the quantum proof and acceptable methodologies for establishing values for these terms. The proposal similarly obscures the precise calculus for determining whether injury is indeed outweighted by costs. For example, assume a seller misrepresents the actual performance capabilities of its product in order to reduce production costs and price, and at the same time increase market share. Will the seller be freed of liability if 10 percent of the products malfunction where the cost of replacing the units is substantially less than the aggregate price reduction distributed to the other buyers? This can hardly be so. Nevertheless, similarly foolish notions will be litigated in the event the Congress adopts these ill-conceived cost-benefit proposals.

We acknowledge that cost-benefit analyses can be very useful as an administrative policymaking tool. As a case selection criteria, it is frequently used in our office to determine the proper allocation of the Commonwealth's resources. However, cost-benefit analysis is unworkable in the context of individual adjudications by the FTC or state courts. We agree with Chairman Miller's comments in his March 5, 1982, letter to this committee: "As to the element pertaining to the weighing of benefits and costs, however, the Commission believes there is an associated problem to consider, namely the risk that the analysis might unnecessarily complicate and delay an investigation or an ultimate litigation. For this reason, the Commission believes that a highly quantitative benefit/cost analysis may not be appropriate in each and every individual case, and that in some cases a far more subjective analysis would be the reasonable approach."

Certainly a "highly quantitative benefit/cost analysis" will complicate and delay investigation and litigation. Both the government and a business will expend much time and effort in ascertaining the ratio of costs to benefits of a questioned practice. Whatever the result, it is hard to imagine that the investigation and litigation process will be less burdensome with these added factors than under the present law. To the extent that these suggestions to modify section 5(a) are an attempt to lessen the burden on business, the statute will not have that effect.[4]

B. ACTUAL INJURY/MATERIALITY

It has also been proposed by Mr. Miller that a practice should not be considered deceptive unless it causes actual consumer injury. To this end, he proposes that a materiality requirement be incorporated into the law of deception. The implications of this proposal are unclear. In *FTC* v. *Colgate-Palmolive Co.,* 380 U.S. 374, 392 (1965), the Supreme Court confirmed that for an advertisement to be deceptive, the Commission must find that it will be a material factor in a consumer's decision to purchase a product. However, the Court noted that the Commission need not survey the public to support such a finding, but may infer materiality from all the evidence. Thus, while materiality is already an element of deception, Mr. Miller apparently desires to alter the burden of proof.

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[4] Chairman Miller's suggestion that a "subjective analysis" is more reasonable certainly makes sense theoretically. However, the fact that none of the legislative proposals reflect this type of analysis suggests very persuasively that these subjective criteria are not properly part of a statutory rule of law.

As we have noted above, a requirement of actual proof of injury beyond that already required is both burdensome and impractical. If an advertisement is demonstrably and materially false, the law should not permit its publication. Sophisticated measurement of the effect of the extent of actual injury is unnecessary.

C. FACT VERSUS OPINION

The proposal to limit "deception" only to statements of fact reveals a shocking lack of sensitivity to the vulnerability of consumers in an increasingly complex marketplace, and lack of familarity with developments in the common law in this area in the 20th century.

It has long been considered a fundamental rule of law of the common law that a statement of opinion does not support an action for misrepresentation, on the grounds that a mere statement of belief does not imply knowledge on the part of the speaker. In the case of harmless puffing, this is clearly true. Thus, representations by an auto dealer that a car is a "dandy", a "cream puff", or the "top of the line" are not generally statements upon which consumers will rely. However, a leading scholar on the law of torts has pointed to a crucial reality: "The puffing rule amounts to a seller's privilege to lie his head off, so long as he says nothing specific . . . . It is not surprising therefore, that the rule has not been a favored one . . . ." Prosser, Law of Torts, p. 723.

In fact, the common law rule that opinions are not a basis for relief is riddled with exceptions. Courts have long recognized that an expression of opinion may carry with it an implied assertion that the speaker knows facts supporting the opinion. E.g., *Shepherd* v. *Kendrick,* 236 Ala. 289, 181 So. 782 (1938); *Ward* v. *Jerson,* 87 Ore. 314, 170 P. 538 (1918). When the parties do not purport to be dealing on equal footing as to available information, the basis for the individualistic approach of the common law [which assumes equal bargaining strength] is destroyed. Prosser, p. 727. Indeed, the courts permit recovery for deceit resulting from an expression of opinion even where the disparity in knowledge or understanding arises from illiteracy or ignorance. As applied to consumer transactions, the law of deception under the FTC and various state acts correctly assumes that there is an informational imbalance between consumers and business. *E.g., Commonwealth* v. *DeCotis, supra.* In determining whether a particular representation is deceptive, or mere puffing, both federal and state law examine the effect of the statements. A misrepresentation which may have the effect of inducing consumer purchases is deceptive regardless of whether it is framed as an opinion. *E.g. FTC* v. *Colgate-Palmolive Co.,* 380 U.S. 374 (1965); *Kugler* v. *Koscot Interplanetary, Inc.,* 120 S.J. Syper 216, 293 A2d 682 (1972). Since, therefore, the common law and the law of deception have developed a consistent approach to the distinction between fact and opinion, we see no reason to change or modify § 5(a).

D. REASONABLE VERSUS IGNORANT CONSUMERS

It is well established state and federal law that an act is deceptive if it has the capacity or tendency to deceive even the ignorant, unthinking, or credulous consumer. Chairman Miller has suggested that the Congress define "deception" to reach only acts or practices which are likely to deceive reasonable consumers. In the case of particularly vulnerable consumers, he would impose liability only if the business knew or should have known of the likelihood of deception. These proposals are puzzling, as we are not aware of any commentary in legal or trade publications critical of the prevailing state and federal standards. Moreover, the current rule ensures a broad, uniform application in the context of mass marketing techniques.

This attempt by Mr. Miller to limit the protections of the Act to certain consumers only will not work in the "real world" of state and federal law enforcement. The proscription in § 5(a) and the various state statutes against "deceptive" acts or practices is applied by the FTC and state attorneys general to practices affecting relatively large classes of consumers. This suggested change in the law would require prosecutors to prove the reasonableness of consumer conduct. Predictably, it would require years of case by case adjudication to define standards of reasonableness, as well as acceptable methodologies of proof. Would reasonableness of consumer conduct be determined for the class of consumers injured by a practice as a whole, or would the law differentiate in degree among various consumers depending on the complexity or sophistication of the product or marketing scheme in relation to the age, intelligence, and prior purchasing experience of the individual consumers in the class? While a boon to the legal profession, these and numerous additional questions would confound the FTC and state court judges, seriously undermine the orderly development of the law of deception, and strap the resources of federal and state consumer protection officials.

Similarly, Mr. Miller's proposal would also hamper enforcement of individual consumer rights in the context of private civil action for damages. In the case of private actions, the courts often insist on a causal connection between the deceptive act and the consumer injury. While proof of actual reliance is not required, *State* v. *Ralph Williams' North West Chrysler Plymouth, Inc.*, 87 Wash. Fed. 298, 553 F2d 423 (1976), *Slaney* v. *Westwood Automotive*, 366 Mass. 688, 322 NE 2d 768 (1975), the deceptive act or practice must be a material element or factor in the resulting injury. *Cf., Kohl* v. *Silver Lake Motors*, 369 Mass. 795, 343 NE 2d 375 (1976). As applied to these individual plaintiffs, Mr. Miller's proposal would impose a new and difficult element of proof which would often shift the focus of the litigation from the deceptive act or practice of the business to the conduct of the consumer. Presumably, the standards of business conduct, rather than being uniform, would vary depending on the knowledge, sophistication, and experience of the consumer.

In a practical sense, we agree that the case selection criteria applied by federal and state prosecutors should consider whether consumers should have been expected to avoid the deception. In fact, we believe that federal and state agencies very carefully evaluate whether it is appropriate for government to advocate the cause of certain consumer injuries. While agencies do not always make the best decisions, it is no answer to misguided prosecutions to tinker with a proven legal standard and render it virtually unworkable.

The deficiencies in Chairman Miller's proposal are even more apparent when considered in light of his "safety net" for vulnerable consumers. Under longstanding interpretations of § 5(a) and the parallel state statutes, a practice is deceptive if it has the capacity to deceive any substantial or appreciable segment of the public. Thus, the FTC and the courts have created a uniform minimum standard of conduct which properly encompasses all likely targets of a marketing effort by a particular business. Under this standard, state courts have readily held that particularly vulnerable groups of consumers are protected from the deceptive impact of certain sales practices, including non-English speaking, uneducated consumers, *People* v. *Conway*, 42 Cal. App. 3d 875, 117 Cal. Rptr. 251 (1974), uneducated minority groups, *Kugler* v. *Romain*, 58 N.J. 522, 279 A2d 640 (1971), and the sick or handicapped, *Commonwealth* v. *Handicapped Industries, Inc., supra.*

Mr. Miller proposes that the law recognize a dichotomy between reasonable and vulnerable consumers. Average consumers who act reasonably are apparently protected regardless of whether the business knew of the likely deceptive effect of its marketing. Vulnerable consumers who act in an unreasonable or gullible manner, on the other hand, are protected only if the merchant knew or should have known of the effect of the practice. It is unclear how high the threshhold of reasonableness rises. Of course, the stricter the standard, the larger the segment of the public who must qualify as vulnerable consumers to invoke protection of the law (and even then only in the case of a showing of knowledge).

Again, it would take years of litigation to restore any semblance of stability or predictability to the law, as the FTC and the courts seek coherent definitions of reasonableness, vulnerability, and knowledge. More importantly, these proposals are designed to substantially reduce the standards of acceptable business conduct. If Mr. Miller's proposal is adopted, the elderly, the sick, the handicapped, and other regular targets of deceptive practices will suffer their economic losses in face of defenses of good faith, or lack of intent or knowledge.

III. CASE EXAMPLES

The implications of the proposals to amend § 5(a) are illustrated by two examples of the operation of the current law of deception at the state level:

A. CASE 1

During 1981, the Massachusetts Attorney General became aware of a serious problem concerning adjustable or variable rate home mortgage loans extended by two local banks during 1976–1977. An investigation revealed the following facts:

The banks aggressively marketed a variable interest rate which was approximately 1 percent—1½ percent below the prevailing rate for conventional, fixed rate agreements to 1,200 Massachusetts residents. At the time of the mortgage application, prospective mortgagors were told that the interest rate could be increased every 5 years by no more than ½ percent. At the time of the closing, buyers were provided for the first time with Truth-In-Lending disclosures, and a copy of the mortgage agreement and note. These documents disclosed that the actual agreement between the buyer and the bank was for a 5 year mortgage amortized on a 25 year basis, with a balloon payment due at the end of 5 years. The promisory note was a simple demand instrument for 5 years.

Many of the 1,200 buyers were not represented by counsel, and did not understand the implications of the actual agreements executed on the day of closing. Others inquired of the loan office and bank counsel concerning the apparent discrepancy between the "net impression" previously created by the bank and the loan documents. These inquiring buyers were told that the instruments were drafted in this manner to simplify foreclosure in the event of default by the borrower. They were assured that the bank had every intention of renewing the loan at five year intervals if the borrower made timely payments on the note. Not suprisingly, in light of the emotional and financial commitment to completing the transaction, these "informed" buyers executed the mortgage instruments.

The initial 5 year rate on the 1,200 loans ranged from 7½ percent to 9½ percent. In 1981, with mortgage rates at 18 percent, the banks began to demand payment in full on the mortgage notes as the 5 year terms expired. Many of the 1,200 mortgagors were not financially eligible for refinancing at current market rates and would, in fact, lose their homes if the mortgage notes were called. However, using our state consumer protection law, we were able to intervene and reach a favorable settlement for these 1,200 homeowners.

This result could not have been reached under the traditional law of contracts or fraud. In Massachusetts, as elsewhere, contract law is too limited and the law of fraud too stringent to prevent this behavior and save these 1,200 homes. However, if the law of unfair or deceptive practices were to change in Massachusetts in accordance with the present proposals, the consumers in a case like this might be defenseless. The banks acted in good faith, with no intent to deceive. They did not know that interest rates would more than double and it was not foreseeable that market conditions would virtually compel them to call the loans. Our extensive investigation never clarified whether the consumers acted "reasonably". These homeowners covered the spectrum from investment analysts to uneducated first-home buyers. All of them were deceived to some extent, though some much more completely than others. The costs and benefits are impossible to quantify. Analysis of "costs vs. benefits" would depend on banking conditions 5 years ago, the length of time each consumer planned to stay in the home, and the fluctuating cost of funds over a 25 year period. Such an analysis would be difficult and lengthy, if even possible. We feel that this type of analysis would be totally inappropriate in a case such as the home mortgage one described.

B. CASE 2

The Massachusetts Consumer Protection Act has dramatically changed traditional business practices of real estate brokers in Massachusetts. Until quite recently, real estate brokers routinely made representations of fact or opinion concerning residential homes, particularly concerning matters of common interest to prospective buyers such as drainage conditions, or the quality of the furnace and roof. Examples include statements such as: "I've been in this business for 20 years, and that roof should go another 10 years", "The boiler is in tiptop condition" or "This parcel contains 4.5 acres."

While many of these representations were perhaps made in good faith, and in the belief that a "sale" demanded in aura of all-knowing professionalism, many buyers in Massachusetts were injured when the representations upon which they relied proved to be false. After a series of decisions which established such representations were deceptive under the consumer protection statute, the accepted approach to real estate practices changed, Today, knowledgeable brokers do not make representations of fact or opinion about matters of which they have no personal knowledge or expertise, nor do they convey information from the seller or other than a third party concerning the property without disclosing the source of the information and whether it has been independently verified by the broker. No longer does the law punish injured consumers by predicating liability on what the broker knew or intended by his representation or statement of opinion.

Mr. Miller's proposal to restrict protection from deceptive practices to "reasonable" consumers would upset the uniformity of business conduct generated by the Massachusetts statute. Unscrupulous brokers could "size up" prospective purchasers before determining what type of representations would "pass" under the law. This approach should not be allowed.

IV. CONCLUSION

It has been only 15 years since the federal government first encouraged the states to embark on a new course to protect consumers. The legislature of all 50 states have decided to follow the federal example embodied in § 5(a). Consumers and honest business people in every state are well protected in the marketplace by the operation of these statutes. Before Congress takes any step to alter the underlying federal law, it should study the impact of its actions. We see no reason, as part of an effort to curb the jurisdiction of the FTC, to jeopardize the enforcement of state consumer laws.

EXHIBIT A.—TABLE OF STATE STATUTES [1]

[State Deceptive Practices Acts]

Jurisdiction	Statutory cite (et seq.)	All § 5 prohibitions	Unfair or deceptive practices	Deceptive practices only	Private actions
Alabama	Alabama Code Title 8 § 19-1			X	X
Alaska	Alaska Stat. § 45.50.471	X		X	X
Arizona	Arizona Rev. State § 44-1521			X	
Arkansas	Arkansas Stat. Ann. § 70-901			X	
California	California Civ. Code § 3369 (Deering); Cal. Bus. & Prof. Code § 17500 (Deering).		X	X	X
Colorado	Colorado Rev. Stat. § 6-1-102			X	X
Connecticut	Connecticut Gen. Stat. § 42-110	X			X
Delaware	Delaware cod tit. 6, § 25		X		
District of Columbia	District of Columbia Code tit. 28 App. § 1.		X	X	X
Florida	Florida Stat. § 501.201	X			X
Georgia	Georgia Code § 106.1201		X	X	X
Hawaii	Hawaii Rev. Stat. § 481A	X			X
Idaho	Idaho Code § 48-601	X		X	X
Illinois	Illinois Rev. Stat. ch. 121½, § 261	X			X
Indiana	Indiana Code § 24-5-0.5			X	X
Iowa	Iowa Code § 713-24			X	
Kansas	Kansas Stat. § 50-623			X	X
Kentucky	Kentucky Rev. Stat. § 367.110		X		X
Louisiana	Louisiana Rev. Stat. Ann. § 51:1401 (West).	X			X
Maine	Maine Rev. Stat. tit. 5, § 206	X			X
Maryland	Maryland Com. Law Ann. § 13-101		X	X	X
Massachusetts	Massachusetts Gen. Laws Ann. ch. 93A	X			X
Michigan	Michigan Comp. Laws § 445.901		X	X	X
Minnesota	Minnesota Stat. Ann. § 325.771 (West).			X	X
Mississippi	Mississippi Code Ann. § 75-24-1	X		X	X
Missouri	Missouri Ann. Stat. § 407.010			X	X
Montana	Montana Rev. Codes Ann. § 85-401	X			X
Nebraska	Nebraska Rev. Stat. § 59-1601	X			X
Nevada	Nevada Rev. Stat. § 598-360			X	
New Hampshire	New Hampshire Rev. Stat. Ann. § 358-A:1.	X		X	X
New Jersey	New Jersey Stat. Ann. § 56:8-1 (West).			X	X
New Mexico	New Mexico Stat. Ann. § 49-15-1		X	X	X
New York	New York Gen. Bus. Law § 349 (McKinney).			X	
North Carolina	North Carolina Gen. Stat. § 75-1	X			X
North Dakota	North Dakota Cent. Code § 51-15-01			X	
Ohio	Ohio Rev. Code Ann. § 1345.01 (Page).		X	X	X

Footnote at end of table.

EXHIBIT A.—TABLE OF STATE STATUTES [1]—Continued

[State Deceptive Practices Acts]

Jurisdiction	Statutory cite (et seq.)	All § 5 prohibitions	Unfair or deceptive practices	Deceptive practices only	Private actions
Oklahoma	Oklahoma Stat. Ann. tit. 15, § 751 (West).			X	
Oregon	Oregon Rev. Stat. § 646.605		X	X	X
Pennsylvania	Pennsylvania Stat. Ann. tit. 73, § 201-1 (Purdon).	X		X	X
Rhode Island	Rhode Island Gen. Laws § 6-13.1-1	X		X	X
South Carolina	South Carolina Code § 39-5-10	X			X
South Dakota	South Dakota Compiled Laws Ann. § 37-24-1.			X	X
Tennessee	Tennessee Code Ann. tit. 47-18		X	X	X
Texas	Texas Bus. & Comm. Code Ann. tit. 2, § 17.41 (Vernon).			X	X
Utah	Utah Code Ann. § 13-11-1			X	X
Vermont	Vermont Stat. Ann. tit. 9, § 2451(a)	X			X
Virginia	Virginia Code § 59.1-196			X	X
Washington	Washington Rev. Code § 19.86.010	X			X
West Virginia	West Virginia Code § 46A-6-101	X		X	X
Wisconsin	Wisconsin Stat. Ann. § 100.20	X			X
Wyoming	Wyoming Stat. § 40-102			X	X

[1] This exhibit and other portions of the testimony reflect information received subsequent to the hearing.

Senator KASTEN. Mr. James DeLong.

Mr. DELONG. Thank you, Mr. Chairman. My name is James DeLong. I am an independent lawyer in Washington and I am not appearing here on behalf of anyone. I am here because I have been involved in this issue for a number of years and in a variety of contexts, and my major purpose is to provide some historical perspective.

I was an Assistant Director of the Federal Trade Commission's Bureau of Consumer Protection, working primarily on rulemaking proceedings, from 1974 to 1977. I was the Research Director of the Administrative Conference of the United States during the period when it was conducting its study of the FTC. More recently, I have been an occasional consultant to the Director of the Bureau of Consumer Protection of the FTC. In this capacity I have discussed some of these issues involved in statutory change with the FTC staff.

I will state my conclusions very briefly, as the Committee desires. It is important to recognize that this issue of section 5 and the guidance it gives to both the Commission itself and to the outside community is one that has been a matter of very intense concern within the FTC since at least 1975, starting very soon after the Magnuson-Moss Act was enacted.

The problem that I saw at that time, when I was there trying to implement this statute, and the problem I see still, is that section 5 is really too vague to give any internal guidance. This made it very difficult for the Commission to tell me or for me to tell my staff what a good case was and what it was not. It led to a lot of rulemakings in which one simply developed hypotheses about why a particular practice might be unfair or deceptive, and then proceeded on the assumption that the hypotheses were in fact true. Because the statute gave us no criteria against which to test our hypotheses, we tended to fall into the trap of trying to confirm them rather than test them, a subtle but important difference.

This in turn had a terrible impact on the kinds of evidence we sought. Many rulemaking proceedings depended almost totally on anecdotes. There was little in the way of solid statistical evidence, surveys or, in general of the types of evidence that really ought to be persuasive to someone involved in making a general rule. Much of this was traceable quite directly to the fact that section 5 placed no effective limits on the hypotheses one could erect and then try to make stick.

Now, these problems have been written about at considerable length by many people, including many Commission staff people. A number of excellent articles have been produced over the last 3 or 4 years. The consensus, I think, is that section 5 does indeed need better definitions.

The question in my mind is whether it is worthwhile to do this by statute, or whether the Commission itself has not already taken the steps necessary for this process of redefinition. On balance, my view is that it would be wise to do it by statute.

My reasons are relatively simple. I think it is important to the Commission itself to reach some closure with the Congress on these issues. It is obvious that Congress has been unhappy with many of the results here. It seems to me that the past couple of years have seen a very useful dialog, and it seems to me that it is now time for the Congress and the Commission to enter into a new contract that specifies what it is you want the FTC to do. That, I think, will also make oversight much more productive.

My view that statutory change is desirable is also based heavily on my strong opposition to a system in which Congress makes a vague delegation and then, by legislative veto, exempts particular persons from the consequences. A fundamental principle of delegating authority to agencies is that their rules should apply evenhandedly, without special exemptions.

Now, of course, the question of just how to define the statute is considerably tougher. I might say that in the past 5 years, and in the volumes of literature which I could show you, no one has succeeded completely in developing a precise definition. There is simply no way in which you are going to create a statute for the FTC that does not leave the agency with substantial discretion and with the responsibility to exercise that discretion intelligently.

I do think that opinion seems to be coalescing around the concepts presented in the December 1980 policy statement, and this seems to me a reasonable compromise between the desire on the part of some people to really pin the Commission down and the desire on the part of others to leave it maximum flexibility. These concepts focus attention on the facts that the Commission is primarily an economic regulatory agency—that its primary responsibility is to insure that consumers can make the choices they want to make in the marketplace, and that that marketplace is functioning properly.

In its antitrust context, of course, the Commission protects the market against practices which harm competition. In consumer protection it tends to worry about information or about situations where sellers systematically violate people's contract rights on the theory that the victims cannot afford to sue. There is a whole economics of information that is being developed in large part by the Commission's own Bureau of Economics which is going to be very fruitful in the future.

It seems to me that focusing on the idea that significant consumer injury has to occur, that it not be avoidable, and that it be not outweighed by benefits is a reasonable and not unduly restrictive guideline to the Commission.

On the deception point, people are concerned because the "tendency or capacity to deceive" test, when combined with the idea of protecting even the most irrational consumer, contains no limits. Under this test, any ad, or even any failure to disclose information, could be regarded as deceptive. The business community feels that this puts them totally at the mercy of the Commission and its discretion and they would like more certainty there.

Again, it seems to me that the idea of defining deception more precisely will provide this certainty. More importantly from my point of view, it would provide the criteria the Commission and its staff need to function effectively. The Commission would still have ample authority to protect vulnerable people who are in fact targeted by unscrupulous sellers.

I will stop there and let the panel go on.

Senator **Kasten**. Mr. DeLong, thank you very much for your testimony. Mr. Mark Silbergeld, who is the director of the Consumers Union. Mr. Silbergeld.

Mr. **Silbergeld**. Thank you, Mr. Chairman. I would like simply to submit my prepared statement for the record. Rather than even summarizing the statement, although I do want to mention a couple of things that are in there, I would like to focus on the unprepared—or at least, the unwritten—part of Chairman Miller's presentation yesterday. We are very concerned about the question of changing the standards of deception, and we think you ought to know that the presentation you heard yesterday does not substantiate the recommendations that it accompanied.

First, however, I would like to say that I agree with Mr. DeLong. There is a consensus forming that the standards for unfairness are those identified in the Commission's letter to Senators Ford and Danforth of December 1980. And I agree with him also that the question is whether or not that should be codified. But I do not reach the conclusion that it should be.

I do not think what you would have, would be a new contract between the Congress and the Commission. Rather, I think what would happen is that you would assume, having done that, you on the Committee and Members of Congress generally, would then expect to agree with everything the Commission did under the unfairness doctrine. And every time the Commission brought a case that some Member did not understand or simply did not agree with, there would be the accusation that despite the Commission having been given a new charter it was now off on its own again.

And so, I am not sure that political question gets settled by codifying. I am afraid what you get primarily by codifying is raising those standards to a statutory level that judges must enforce in every case, because they then become elements of the case, with a tremendous amount more litigation, more lawyering in the case, than you would have if they were simply guidelines.

I think the committee ought to rest on its laurels. It has gotten a clear statement from the commission of how the Commission applies that doctrine and what the Commission believes the elements of unfairness to be. The Commission has put it in the public record, and I think the Commission intends to stick to that, and I think the committee is to be commended for getting that job done.

I recommend that you rest there instead of creating many years of unnecessary additional litigation by putting it into section 5.

Now, I should say with respect to deception, it is remarkable that the business community has not, during the several years of debate over whether the Federal Trade Commission has been faithful to its statutory charge, complained about application of the deception language in section 5. And yet, the Chairman of the Federal Trade Commission appears before this committee and asks that it be changed and cites several examples to support the bases upon which he recommends change.

After the chairman's testimony was completed yesterday, I went over to the Federal Trade Commission, and then back to my office, on the phone to get a list of the cases that supposedly are the examples justifying the change in the statutory provision against deception.

That list, as of 5:30 last night, did not exist, let alone did any written analysis exist. And while I do not say that to suggest that the Chairman Miller does not have cases in mind, I say that to suggest that the analysis is rather slipshod. So let me take a look at the 10 examples that were presented to the committee yesterday.

I think you will agree when you hear these, that they do not justify the proposed change in the standards by which deception should be measured; 5 of the 10 examples were 1962 or earlier cases. The hair color case was *Clairol,* 1941. The yogurt case was *Dannon,* 1962. The oldest of them, the deodorant case, was *In the Matter of Sibone,* decided in 1943. The cigarette case was *Liggett & Myers* in 1958, and the foreign origin cases, I have been unable to find any that have been brought since the early fifties.

Two of the lines of cases involve the matter of *Jim Miller* v. *Consumer Preference*—the re-refined oil case, and the foreign origin cases follow longstanding trade regulation, doctrines affirmed by the Supreme Court, that buyers are entitled not only to equivalent value for their money, but also to get what the advertiser said they were going to get.

We now have a conservative economist coming before the committee, departing from conservative economic doctrine by saying that consumer preference is not sovereign in the marketplace. That is a remarkable recommendation.

What is worse is that 5 of the 10 examples involved a misreading or careless analysis of the cases. The safety Champion claim for Firestone tires was not the major claim in the case. Firestone lost that case because they were found to be unable to substantiate the claim that their tires stopped 25 percent faster.

That was the issue in the case, and to pick on—although you may disagree with the lawyer's technique of adding other counts once you have decided you are bringing a case. Mr. Miller cannot support the claim that the Commission would have brought that case simply to challenge the trade name issue. The case was brought primarily, and won primarily, because Firestone could not substantiate an objective performance claim.

In the yogurt case it was suggested that the Commission brought that case because it did not like the characterization "yogurt is nature's perfect food." In fact, that claim was made in context with three claims that yogurt would relieve or cure gastrointestinal symptoms. It was a serious case. It involved objective health claims. The Commission won that case and the claim in that context is not frivolous and it does not justify a change in the standards for deception.

The *Chevette* case, there was a consent order in that case signed by the Chevrolet Division, but in fact, the Commission staff was prepared to show, had the matter gone to trial, that consumers viewed that ad not as an ad in which the opinion of Road and Track magazine was presented, but that presentation of that opinion constituted Chevrolet's own objective performance claim as to the handling of the car. And in fact, whether or not Chairman Miller understood that as a performance claim, although there is some subjective professional expert witness judgment involved, car handling is a matter which is primarily measured by objective standards. Such things as cone-swerve tests.

The *Everlasting Stockings* case, which he offered as a matter of ridicule because people understand stockings do not last forever—the administrative law judge found that people read that ad to mean simply that the stockings were of high quality and comparatively durable compared with other products and, in fact, they were being sold by mail orders so you could not see them in advance. And it was found that they were, in fact, not high quality products or that their quality was being greatly misrepresented.

You might quibble with whether that is the case the Commission wants to bring, but it certainly does not justify changing the standards of deception because it certainly does not represent a case where the Commission was attacking a claim based on the assumption that the public is subject to persuasion by any foolish statement.

The cigarette case—"our cigarettes taste milder"—that was the *Liggett & Myers* case. In fact, that claim was found by the administrative law judge to be read by the public as a claim for a less irritating cigarette. This was prior to the low tar cigarette. The industry was focusing its large national ad campaigns on their brands being less irritating to the throat, which in fact is an objective medical kind of claim.

The industry thought it was the most important selling point to the public, and the administrative law judge found that the public thought that was not a subjective claim but in fact, a claim that fit right in with the main focus of the industry's ads at the time. And so that was not a foolish case of attacking an opinion claim; that was a case which went to the heart and the focus of a large national industrywide ad campaign.

Now, as to a handful of gullible people, I think the chairman is off base again. The handful of gullible people who believe, as I suggest in my prepared statement, that somebody's packaged white powder to sprinkle on your living room rug will cut your heating bills in half probably ought not to be protected by Federal Trade Commission resources.

The handful of gullible people who were fooled in the *Aaronburg* case which is cited in my testimony into thinking—women into thinking that this product would take care of their problems with delayed menstruation when, in fact, the product produced severe abdominal cramps and spontaneous abortions in women whose menstrual delay was due to as-yet undiscovered pregnancy, perhaps are a handful of people that ought to be protected even if they are gullible.

I do not think that you can simply write into the statute an exclusion for the "handful of gullible people" cases because one of the questions is what are the consequences of gullibility. And another of the questions is what was the intent of the advertiser.

And so, I think that with respect to Chairman Miller's recommendations as a whole, you have to be very careful about the suggestion that there are cases in the Commission's recent history that show that the Commission is in the process of misallocating its resources in bringing foolish cases. I will provide my analysis of his 10 examples for the record.

Now, I will close in a second, but I would just like to say with respect to the McClure-Melcher recommendations to modify the definition of deception, that in addition to what Mr. Montgomery said about it with which I fully agree, business marketing professionals, trade regulation lawyers, and consumers will be left in a state of total confusion if the question of whether or not an ad is deceptive has to be measured by its aggregate effect of cost and benefits on customers of a company and on that aggregate effect combined with the effect on competition.

That would turn every little false and misleading advertising case into an antitrust case that can be down there at the Commission, litigated with expert economic witnesses for years. If what you want to do is change the marbles in the *Campbell's Soup* case into the cereal case, the best way to do that is to adopt the McClure-Melcher definition of deception.

With that, Mr. Chairman, I close.

[The statement follows:]

STATEMENT OF MARK SILBERGELD, DIRECTOR, WASHINGTON OFFICE, CONSUMERS UNION

Mr. Chairman and Members of the Subcommittee, Consumers Union appreciates this opportunity to state its views on S. 1984, the proposed Federal Trade Commission Amendments, which proposes to reauthorize the Federal Trade Commission, and on the subject of FTC's operating authority. We are joined in this statement by National Consumers League, which has appeared many times before this Subcommittee. NCL will submit additional views for the record.

This testimony will address the question of the FTC's authority to act against "unfair or deceptive acts or practices" as provided in Section 5 of the Federal Trade Commission Act. We will later submit for the record additional views on other major issues likely to be considered by the Subcommittee in acting to reauthorize the Commission. Among other things, we will: Oppose exemption from FTC jurisdiction of acts and practices of the licensed professions; Oppose extension of the current prohibition on FTC rulemakings that apply an unfairness standard to commercial advertising, and oppose further application of this prohibition to quasi-adjudicative proceedings; and recommend deletion of the existing legislative veto provision added to the Federal Trade Commission Act by the amendments of 1980.

The Federal Trade Commission is an essential force for fairness in the national marketplace for consumer goods and services. It is charged by law with prohibiting unfair or deceptive acts or practices and unfair methods of competition. While limited resources obviously prohibit the FTC from eradicating such marketplace conditions, most would admit that on the whole the marketplace is more honest, more fair and more competitive because since 1914 we have had an FTC.

The Commission's reach into the marketplace is not restricted by its own limited resources. The effect of the legal standards it establishes in promulgating rules and deciding adjudicated cases is amplified greatly by the fact that 49 states and the District of Columbia have so-called "Little Federal Trade Commission Acts" that apply at the state and local level FTC standards of unfair methods of competition, unfairness and deception.

Further, many national and regional advertisers and advertising agencies participate in industry mechanisms (including the National Council of Better Business Bureaus' National Advertising Review Board) which apply these FTC standards on a voluntary basis.

It has become fashionable in many quarters to attack the FTC as a bureaucracy out of control, an agency run amok. I suspect, however, that even those who lead such attacks on FTC would—off the record, in a moment of contemplation—concede that the Commission's problem may be that it merely did its job too well. It is under attack not because it violated the letter or spirit of the laws that Congress gave it to enforce in 1914 and 1938,[1] but because of its slowness to read into law a changing political mood conciliatory to most demands of the business community.

UNFAIRNESS

When the Congress in 1980 considered legislation to reauthorize the Commission's authority, it focused heavily on the FTC's power to prohibit unfair acts or practices. In response to industry demands, the 1980 FTC amendments prohibited the Commission from applying its unfairness authority to commercial advertising through the rulemaking process. Exercise of that authority in adjudication was, however, permitted. During the two years for which FTC was reauthorized, the Congress determined, the concept of unfairness would be carefully examined to determine if the term should be subject to some statutory definition or limitation.

This Subcommittee solicited and published in 1980[2] the views of various interested parties regarding the concept of unfairness in Section 5. In aid of the Subcommittee's inquiry, the FTC on December 17, 1980, transmitted to Senators Ford and Danforth a legal analysis of FTC's appplications of the unfairness doctrine to consumer transactions and of related procedural issues.

That analysis identifies five elements that have been used to determine that an act or practice is "unfair" under Section 5 of the Federal Trade Commission Act: (1) the act or practice must cause substantial injury to consumers; (2) the injury must not be outweighed by resulting countervailing benefits to consumers or to competition; (3) the injury must be one that consumers could not avoid; (4) the act or practice must violate public policy; and (5) the act or practice must be immoral, unethical, oppressive or unscrupulous.

The Commission's analysis of how these five elements have been applied is relatively simple. Primarily, the FTC must establish each of the first three elements in order to establish unfairness—substantial consumer injury, unavoidability by consumers and lack of countervailing benefits.

The fourth element normally has been an evidentiary measure of consumer injury rather than a separate, necessary element of unfairness. But where, for example, there is a clear legislative determination that an act or practice violates public policy, that may satisfy without more the need to establish the first three elements.

The fifth element is no longer relied upon by the Commission because the FTC has concluded that this test has proved to be duplicative; conduct that is immoral, unethical, oppressive or unscrupulous almost always injures consumers, by violating clearly established public policy or otherwise.

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[1] In 1914, the Congress authorized the FTC to issue cease and desist orders against unfair methods of competition. In 1938, in order to clarify that the agency's authority was intended to protect consumers as well as competitors, the Congress enacted the Wheeler-Lea Amendment to Section 5. It authorized the FTC to ban, as well, unfair or deceptive acts or practices.

[2] Unfairness: Views on Unfair Acts and Practices in Violation of the Federal Trade Commission Act (1980), U.S. Congress, Committee on Commerce, Science and Transportation, Consumer Subcommittee, (1980), published as a "Committee Print."

The FTC's letter to Senators Ford and Danforth makes clear that the FTC considers these principles to be legal requirements for a determination that an act or practice is unfair. Thus, it seems clear that the FTC's unfairness jurisdiction is adequately defined by legal precedent.

S. 1984 appears to intend that the first three criteria articulated by the FTC be inserted into Section 5 as a statutory definition of unfairness.[3] Indeed, on March 5 the FTC sent a letter to Chairmen Packwood and Kasten, agreeing by a 3-1 vote to the appropriateness of a statutory definition of unfairness based on the December, 1980 analysis.

We disagree that a statutory definition of unfairness is desirable. The primary effect of codification would be to create litigation in unfairness cases over what effect codification adopting all of the elements of unfairness as a definition has had on the Commission's requisite findings in particular cases.

For instance, would codification permit FTC to satisfy the injury elements by finding that an act or practice violates established Congressional policy, since there would be no public policy language in the codification? How would the FTC be permitted to balance short term consumer injury with long-term and largely speculative promotion of competition? If an act or practice injured some consumers and benefited others, could the FTC take into account that the injured were primarily members of a vulnerable group, if that were the case; or must a dollar of benefits and a dollar of injuries be treated equally? What if in a given case there were great injuries to a few people resulting in small benefits to many others, but the aggregate benefit slightly outweighed the aggregate injury?

In view of these questions and may others, it is doubtful that codification will provide the absolute certainty that seems to be the goal of its proponents. We believe that by obtaining clear FTC identification of the standards against which it intends to measure the unfairness of acts and practices in the marketplace, the Subcommittee has achieved a substantial purpose. It should rest on that achievement without changing Section 5 manner likely to create uncertainty, confusion and a generation of unneeded litigation.

DECEPTION

Until just recently, there was no criticism of the legal standards for measuring deception, as that term has been construed under Section 5 of the Federal Trade Commission Act.[4] Advertisers, the advertising profession and the media focused their criticism of the FTC's application of the statutory language "unfair or deceptive acts or practices" solely on the term "unfair."

Indeed the suggestion that such a problem exists seems completely belied by the action of the Congress in its treatment in the 1980 reauthorization of the FTC's so-called "kidvid" (Children's Television) rulemaking. The Commission was prohibited from continuing that proceeding on the basis of the unfairness doctrine, but was permitted to continue, should it decide to do so, on the basis of the doctrine of deception.

Nonetheless, FTC Bureau of Consumer Protection Director Timothy Muris recently informed an apparently surprised delegation from the American Advertising Federation, in a private meeting, that business has a problem it doesn't even know about.

According to Mr. Muris, business's focus on the unfairness doctrine is short-sighted. According to him, Section 5 of the FTC Act gives FTC a great deal—impliedly, too much—leeway in dealing with certain kinds of advertisements. Among these are advertisements that may deceive though not intended to do so, advertising claims based on opinion instead of on fact, and practices that may affect only a handful of gullible people.[5]

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[3] If that is the intent of the bill, it falls short of its mark. The third criterion, avoidability of injury, is missing. As well, there are drafting errors. For instance, the last clause of the single sentence that Section 6(a) of S. 1984 would adopt as the definition fails to refer to a "practice" as well as an "act." And the inconsistency in capitalizing the word "act" in its two meanings gives rise to the curious semantical possibility that the FTC could declare S. 1984 to be an unfair act or practice.

[4] S. 1984, Section 6(a), introduced December 16, 1981, proposes a single definition for unfair methods of competition, unfair acts or practices and deceptive acts or practices. However, the accompanying floor statement addresses solely the issue of FTC jurisdiction over the licensed professions. Given the aforementioned drafting defects in S. 1984 (see note 3, above), we assume that the authors had no specific purpose in mind in proposing a new legal standard for defining deceptive acts or practices, and that inclusion of deception in the proposed new definition was a drafting error.

[5] Advertising Age, March 1, 1982, p. 1.

S. 1984 would impose upon allegedly deceptive acts and practices a cost-benefit test. It would not, however, place the kinds of limitations that Mr. Muris's statement seems to suggest. Neither Mr. Muris nor the FTC Commissioners has prior to these hearings suggested any specific statutory change to deal with the problem he perceives. Given the effect S. 1984 would have on the definition of deception and the possibility that Mr. Muris's suggestions may take on a legislative life, it may be useful to examine what such changes in the concept of deception may do.

The Present Concept. The concept of deception, unlike the concept of unfairness, was not new or vaguely defined when Congress enacted Section 5 of the Federal Trade Commission Act in 1914 or the Wheeler-Lea Amendment to Section 5 in 1938.[6] Deception is based on the concepts upon which the common law and statutory definitions of fraud and misrepresentation, as well as many commercial codes, are also based.

Allowing for the broad range of practices that have been adjudged deceptive under Section 5, deception may be considered a departure from material facts, by commission or omission, in a way that fools someone else.[7]

Despite some variations among Section 5, commercial codes and common law principles of fraud, the concepts that underlie Section 5 are understood by sellers, their advertising agencies, and lawyers for both. To introduce significant change would throw an entire body of law into question and give rise to years of litigation over the application of changed standards to particular cases.

What's more, the fact that these underlying concepts are widely understood is no doubt relevant to the fact that they have not been challenged by the business community. For they are understood in lay terms, if not in technical legal detail, by ordinary people. Responsible businesses understand that they cannot gain in the longrun if acts or practices are condoned by the law that the consumer considers to be in the nature of fraud or deception; such a situation would foster contempt for both the law and business practices.

The Proposed Benefit Cost Definition. The proposal of S. 1984 is that deception be defined as an act or practice which causes substantial consumer injury that outweighs the benefits of that act or practice. The result of this change would be that no one—consumers, advertisers, advertising agencies, FTC, the Congress, or any other interested party or institution—will know until a matter has been before the FTC and the courts what acts or practices are unlawful.

The proposal would destroy sixty-eight years of precedent under Section 5 and centuries of underlying jurisprudence, substituting for basic factual inquiry an economic inquiry based on what most admit is a very inexact methodology. What under the present legal standard of deception is a relatively straightforward examination of the nature and accuracy of a seller's claim in a so-called "F&M" (false and misleading advertising) case would become a complex proceeding similar to an antitrust case.

Sellers and the firms who aid them in their marketing practices would have no certainty as to whether a practice created, on the balance, more harm or more benefit to their customers in the aggregate. And while business interests might suspect that in 1983 they would get decisions more favorable to them in cases of alleged deception, at some future time they could well see the government routinely appear at administrative hearings armed with an array of economic evidence they are unable to match. The pressure to sign consent orders simply because of the government's resource advantages, especially over small businesses, would be overwhelming.

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[6] The term "deceptive" did not appear in the 1914 enactment. But deception was an "unfair method of competition" under the original Section 5. See, e.g.g., *Curtis Pub. Co.* v. *Federal Trade Commission,* 270 F.881 (3d Cir. 1921), aff'd. 260 U.S. 568 (1923); *Federal Trade Commission* v. *Balme,* 23 F.2d 615, (2d Cir. 1928) cert. denied 277 U.S. 598 (1928). The prohibition against "deceptive acts or practices" was added in 1938 to make deception unlawful whether or not it harmed competition.

[7] Deception under Section 5 differs from fraud and some various commercial code concepts in some ways. Intent, for instance, is not a requirement, though it may be present. See, e.g.g., *Federal Trade Commission* v. *Sterling Drug, Inc.,* 317 F.2d 669 (2d Cir. 1963); *Montgomery Ward & Co.* v. *Federal Trade Commission,* 379 F.2d 666 (7th Cir. 1967). And buyers need not actually have been deceived. It is enough that the FTC adjudges the act or practices to have the capacity to deceive. See, e.g., *Perloff* v. *Federal Trade Commission,* 150 F.2d 757 (3d Cir. 1945). This standard makes deception under Section 5 less strict than the typical fraud requirement of detrimental reliance (that is, the customer must have actually relied on the seller's deception, with resulting actual injury).

As to the lack of requirement for the FTC to show actual injury to specific consumers, see *Northern Feather Works, Inc.* v. *Federal Trade Commission,* 234 F.2d 335 (2d Cir. 1956).

On the other hand, the states under Little FTC Acts, and the voluntary advertising review mechanisms of trade assoications, with their comparatively small resources, would be unable to stop some of the most rampant and clearly fraudulent trade practices because of a lack of resources to prepare economic cases. There could result increasing reliance on federal enforcement and an outcry from business and consumers demanding standards of certainty in standards for deceptive advertising that would dwarf recent business complaints about the uncertainty in the doctrine of unfairness.

Proof of Intent. Bureau Director Muris has identified as a problem (at least one he perceives) of Section 5 the lack of any requirement for the FTC to prove intent to deceive. I am unaware of any reason why this should be considered a problem.

That deception under Section 5 is an offense not requiring proof of intent is long-established.[8] I am unaware of any specific enforcement patterns in which the lack of this requirement has beem shown to work an undue hardship or to constitute abuse of administrative discretion. No jurisprudential theory dictates a requirement to include intent as an element of deception—especially since the first penalty for violation of Section 5 is not a civil fine, but only a cease and desist order.

Further, a required showing of intent would greatly reduce the protection that Section 5 affords consumers. This is so both because intent often has no relationship to the injury a deceptive act or practice does to consumers and because the additional resources needed in many cases to prove intent would result in fewer cases, given the same amount of resources.

Finally, I doubt that any business which has even been investigated for an alleged violation involving intent as an element would—given the inevitability of an FTC investigation into its trade practices—prefer to have the kind of investigation that accompanies an enforcement agency's attempts to prove intent. Inquiries (some using compulsory process) of customers, employees, family, business associates and others may become fair game when the government seeks to prove what the business person knew and when he knew it. While the number of investigations probably would decrease because of the greater resources needed to show intent, those who were investigated would probably regret that intent was a relevant issue.

Differentiation of Fact and Opinion Claims. There is no sound basis for differentiating between fact and opinion claims, if in fact that is a correct description of Mr. Muris's suggestion to representatives of the American Advertising Federation. Opinion claims may merely place a factual statement in the words of someone who appears to be stating an opinion. Each of the following can, on the surface, be classified as an opinion claim.

"When I have a very special date, I wear TOXINE, the sophisticated fragrance by Jean-Jacques Fauxpas. When I wear TOXINE, I dare to feel romantic."

"ZIPPY Tomato Cocktail tastes better to me than any sugary soft drink. Picks me up better, too."

"I've driven every car you can buy today, and I think the ZAPSIT 600 handles better than any one of 'em. So take it from Indy Dollars, test drive the ZAPSIT at your dealer soon."

"I expose my skin to the sun's harmful rays ten hours a day on my job. I can't afford painful sunburn or the health risks of too much sun. So when I work, I smooth on BLOXIT."

"When I need to get rid of a headache in an instant, I prefer new, marvelous INSTADRIN. That's because it contains the recently discovered ingredient, snaykoilin, that eight of ten doctors now recommend instead of either aspirin or acetaminophen."

(My apologies to professional advertising copy writers.)

Yet, these five "opinion claims" include only one that presents solely subjective statements of personal taste or opinion (TOXINE). The ZIPPY ad is primarily subjective, as well, but contains a statement that conceivably is ambiguous enough to be construed as also making an objective claim—though not one I think the FTC should spend resources investigating. The ZAPSIT ad presents a claim that can be measured in part by standardized performance tests and in part to some subjective judgement by exports who use or test the product professionally. The BLOXIT and INSTADRIN ads clearly present fact claims in opinion form.

Thus, the distinction attributed to Mr. Muris is one of form, not substance, and it would be a simple matter for advertisers to circumvent a rule that excepted opinion claims from the FTC's deception authority under Section 5. (I am certain Mr. Muris would not want the Bureau to end up in arguments with advertisers about whether their claims were truly fact claims or merely opinion claims in fact claim form—that might be considered a matter of opinion.[9]

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[8] See, e.g. *Koch* v. *Federal Trade Commission,* 206 F.2d 211 (6th Cir. 1953).

The Gullible People. Finally, Mr. Muris reportedly has identified as a problem with Section 5 the ability of the FTC to act against deceptive acts or practices that protect only a handful of gullible people.

There are three problems involved in any attempt to address this "problem" through legislation. One is that there is no meaningful definition of how many people constitute a "handful." The second is that a meaningful federal "gullibility" standard cannot be set. The third is that there are cases in which the potential consequences of gullibility are sufficiently serious to warrant FTC protection of even a handful of gullible people.

Consider, for instance, *Positive Products Co.* v. *Federal Trade Commission.*[10] The respondents in that case marketed by mail order a remedy for use in the event of delayed menstruation. The produce contained ergotin (a vaso-constrictor), aloes, extract of cotton root, black hellebore and oil savin (all strong cathartics and gastro-intestinal irritants). If taken in accordance with the maker's instructions, the product could be dangerous and could cause a spontaneous abortion in women whose menstrual delay was due to pregnancy.

The respondents argued that a careful reading of their advertisements for the product, based on accurate construction of the grammar in its advertisements, showed the product to do no more than it claimed, i.e., relieve *symptoms* of menstrual delay, and did not claim to *remedy* the *causes* of delay. Thus, said the advertisers, the ad was accurate. The FTC, to the contrary, argued that, taken as a whole, the ad would cause most readers to believe the product cured the *cause* of delay, no matter that a literal, grammatically analytical reading of the advertisements supported the respondent's argument.

The Seventh Circuit upheld the FTC's order banning the ads. The court stated:

> The law is not made for experts, but to protect the public—that vast multitude which includes the ignorant, the unthinking, and the credulous, who, in making purchases, do not stop to analyze but too often are governed by appearances and general impressions. . . .

It would be entirely appropriate for the Federal Trade Commission not to spend resources to protect a dozen citizens scattered about the land from believing—and acting upon—advertised claims that that a commercially available powder sprinkled about their living room rug would cut their heating oil bills in half. It does not follow that the FTC should never protect a handful of gullible people, no matter what the consequences of gullibility. Potentially serious injury, intent of the seller, as well as other considerations, may all add up in a particular instance to the conclusion that the Commission should expend resources for such purposes—sometimes. We believe that the Commissioners, and Mr. Muris, as well, are wise enough to know when not to waste resources on foolish cases, and that a directive from Congress is not needed.

SUMMARY

In summary, we oppose the codification of standards for application of the unfairness doctrine because that will lead to substantial additional, unproductive litigation over the issues resulting simply from putting the standard into statutory language. And we oppose any revision of the definition of deception because there is nothing wrong with the term as presently defined in the statute, as well as because the specific proposed changes would wreak havoc in the marketplace.

[The following information was subsequently received for the record:]

ANALYSIS OF CASES CITED BY FTC CHAIRMAN MILLER TO SUPPORT PROPOSAL TO DEFINE "DECEPTION" BY STATUTE

Kroger Co., D.9102 (Commission Opinion dated 11/25/81 not yet published). Kroger Co. ran informal surveys called "Price Patrol" surveys. These purported to compare its prices with prices of competitors and the results, favorable to Kroger, were featured in its advertising. The ads disclosed that the surveys were informal. The Commission determined, by a 3-1 vote, that the advertisements were deceptive, nonetheless, because consumers would view them as methodologically sound and statistically projectible. The case is on appeal to the courts.

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[9] It seems entirely possible that Mr. Muris actually distinguished or intended to distinguish between "objective" and "subjective" advertising claims, a distinction to which Chairman Miller has previously referred. But to date there has been no documentation that FTC inappropriately allocates resources to challenging subjective claims.

[10] 132 F.2d 165 (7th Cir. 1942).

Chairman Miller quotes Commissioner Bailey's dissent to the effect that the decision will chill development of comparative price information useful to the public. At best, this is a decision in which reasonable Commissioners can differ, and it hardly establishes that the Commission should not be permitted to rely on its own expertise to determine the deceptive capacity of an act or practice.

Kroger, at the time it ran these advertisements, possessed two private surveys more scientifically composed and containing much larger sample sizes that the Price Patrol survey. In these, Kroger lost to the competition in market-by-market price comparisons significantly more often that in the informal surveys. Thus, the information advertised clearly could mislead consumers as to the comparative prices of representative marketbaskets purchased at Kroger and at its competitors. Commission Opinion, page 26.

Further, the Kroger official who composed the Price Patrol marketbasket sample also handled discounts from the firm's suppliers and selected price leader items for Kroger's advertising. Three expert witnesses testified that it was not proper to combine these two functions, since to do so creates the opportunity for conscious or unconscious bias of the advertised survey results by permitting selection of advertising leaders as items included in the survey sample marketbasket. This can bias the results in favor of the firm engaging in the comparative advertising.

Block Drug Co., 90 FTC 893 (1977). The Commission challenged claims that Poli-Grip denture preparation would permit the wearer to eat "problem" foods such as apples without discomfort or embarrassement. Chairman Miller argues that the Commission should not have brought the case because the product is cheap and frequently purchased and the claim is easy for consumers to evaluate for themselves. The Chairman's analysis does not identify what elements of his proposed definition of deception would prevent FTC from bringing such cases in the future. It does not appear to be preventable by imposing an actual injury requirement, since the consumer is injured by having to make the initial purchase in order to discover the deception. Indeed, since this kind of claim was common for competing brands of denture cement before the Block case, consumers could buy several brands, compounding the admittedly minor injury suffered in each individual purchase, before deciding that all such claims were deceptive and that the claim was not one on which any brand should be preferred.

Nor would Chairman Miller's proposed "reasonable consumer" standard seem to prevent the Commission from bringing this case in the future, since there is nothing on the face of the claims in this case that would make it unreasonable for a consurmer to disbelieve the claim. And if users of dentures are considered a "vulnerable group" under the proposed Miller standards, then the FTC could argue that the advertiser "should have known" the consumer would be deceived.

This case is at worst one in which the Commission might have found better uses for the resources involved, but hardly substantiates Chairman Miller's request to change the law.

Ford Motor Co., 87 FTC 756 (1976). The advertisement made mileage claims of over 26 mpg's for the manufacturer's five lines of small cars, disclosing that mileage varies according to various factors. The Commission held the claim to be deceptive, despite the mileage variation disclosure. Chairman Miller states that the Commission did so based solely on its own expertise without considering a survey conducted by Ford.

The Chairman's description of the case is, quite simply, incorrect. The Administrative Law Judge considered the Ford survey and concluded that it supported the Commission's, rather than Ford's, argument about the meaning of the advertisement. The fact that the Commissioners on appeal held they were not bound to consider the Ford survey does not mean that it was ignored, only that it was not directly relevant to the narrow issue on appeal and that the Commission still views the "capacity to deceive" doctrine as part of the law. See 87 FTC at 779.

Levitz Furniture Corporation, 88 FTC 263 (1976). This case involved false claims that the advertiser's prices were reductions from its own former prices, among others. Chairman Miller's view is that so long as consumers can compare the prices of the advertised items with the prices for them offered by others, the Commission should not challenge such price claims even if false.

These kinds of cases may not be the best allocation of FTC's resources. Nonetheless, they do not sustain Chairman Miller's argument that they justify a change in the law requiring a showing of actual consumer injury. False pricing claims constitute a deceptive means of a seller's obtaining initial contact with the consumer. There are several reasons why such a practice has long been considered an undesirable trade practice. One is that it often leads to bait and switch practices where the sales situation involves additional oral representations at the point of sale. Further, readers of an advertisement may be unable to compare items with those advertised by others, or may not be interested in the advertisement because of the specific items featured but, rather, in determining which advertisers have comparatively low prices for the type of merchandise offered for sale. False pricing claims may lead customers to the retail premises of those most willing to engage in false pricing claims, to the competitive disadvantage of sellers unwilling to do so as well as to that of the customer. If the advertiser's actual prices are lower or comparable to those of competitors, false claims about the actual prices are not needed to inform customers about prices; while FTC might be unwise to spend resources where there is neither bait and switch nor other actual injury, such practices should not be made lawful simply because in some cases there may be no injury.

Nagle, Spillman & Bergman, Inc., 88 FTC 244 (1976); *Morton-Norwich Products, Inc.*, 86 FTC 299 (1975). In these cases, the Commission challenged, among other things, failure to disclose that potassium chloride products sold as substitutes for sodium chloride (table salt) should not be used by those on potassium-restricted diets. It also challenged, in the first case, the claim that the product tastes like salt.

First, Chairman Miller takes these Commission charges out of the context in which they were made, which is one in which a variety of health and endorsement claims were challenged. Viewers of the ads were invited to diagnose their own hypertension problems and to select the advertisers products as remedies without medical supervision. Next, Chairman Miller fails to state what is defective about a challenge to the failure to disclose—while it may be self-evident to him that the disclosure should not have been required, it is not self-evident. Third, there is no reason to believe that the FTC ever would have challenged the taste claim alone, out of the context of the health claims, so there is no reason that a change in the law would be needed to prevent cases challenging taste claims easily evaluated by consumers themselves.

General Motors Corp., 85 FTC 17 (1975). GM advertised Road & Track magazine's published opinion that GM's Chevy Vega was the best handling passenger car ever build in the U.S. FTC obtained a settlement from GM agreeing not to make such claims without substantiation, after the matter went to trail. GM could not substantiate the handling claim, as contrasted with the claim that Road and Track had stated the views set forth in the advertisement.

Chairman Miller characterizes the Commission's action as having deprived the consumer of valuable information. He states that the Commission apparently thought the Road and Track evaluation was not adequate substantiation. But the evidence in the case shows that viewers of the ad considered GM was asserting the claim as its own factual assertion, not merely as the assertion of another. And GM as an extensive tester of its own cars and those of competitors certainly has the ability to substantiate such a claim if it can be substantiated.

The problem with permitting advertisers to rely on other's opinions about objective performance characteristics is that if the advertiser cannot substantiate the opinion, it can nonetheless shop around for someone who will state an unsubstantiable performance claim in opinion form. Then the door is open to virtually any claim, regardless of the ad substantiation doctrine, which Chairman Miller now states he endorses in principle.

Spiegel, Inc., 82 FTC 20 (1973), 494 F.2d 59 (7th Cir. 1974), cert. denied 419 896 (1974). This is another false pricing case. It is not one that seems to have justified the FTC's use of resources, but the practice should not be made lawful by changes in the concept of deception, for the reasons stated above regarding the Levitz case.

Brite Mfg. Co., 65 FTC 1067 (1964), 347 F.2d 477 (D.C. Cir. 1965). This is representative of a very long and very old line of FTC cases requiring labeling of items of foreign origin where there might be a consumer preference for domestically produced brands of the product. FTC has not brought a case in this line for many years. Further, the preference is not one presumed by the Commission, but one which for many years existed among a substantial portion of the public. Interestingly, Chairman Miller previously has characterized this line of cases as ones FTC should not bring because the purpose of the case was, according to him, to use FTC resources to correct consumers' misimpressions that the domestic item was better. He no longer uses that characterization, since it obviously contradicts his own belief in the sovereignty of consumer preference.

Dannon Milk Products, Inc., 61 FTC 840 (1962). The advertiser claimed the product to be "Nature's perfect food that science made better." Chairman Miller criticizes the case as one in which the Commission took a puffing statement and challenged it as a factual claim.

Chairman Miller takes this characterization of the case totally out of context. The claim was part of advertising that promoted respondent's product as a prevention or cure for various digestive disorders which in fact the product does not prevent or cure. It is another example of his willingness to cite a minor charge in a serious and justified complaint, as if the Commission had based its decision to bring the case solely on such a charge.

Mohawk Refining Co., 54 FTC 1071 (1958), 263 F.2d 818 (3rd 1959). This is representative of the commission's line of cases holding that it is deceptive to fail to disclose that motor oil is used and has been re-refined, if such is the fact. It is an example of *Chairman Miller* v. *Consumer Preference.* He now characterizes the problem with the cases as being that the product performs satisfactorily. He previously has criticized them as using the Commission's resources to correct consumer misimpressions about the satisfactory performance of the product. The U.S. Supreme Court long ago upheld the Commission's position that consumers are entitled not merely to value for their money but to what they believe they are getting. See *Federal Trade Commission* v. *Algoma Lumber Co.,* 291 U.S. 67 (1934). This sort of case may not be the best use of the FTC's resources, but that does not justify changing the definition of deception to render the practice legally non-deceptive. Once advertisers are excused from affirmative disclosures regarding the nature of the product, they also will be free to fool customers as to what they are getting if the performance is adequate, thus substituting seller's judgment for the buyer's judgment—and even the buyer's distinct preference—in the marketplace.

Liggett & Myers Tobacco Co., 55 FTC 354 (1958). The FTC in this case challenged an advertiser's claim that a brand of cigarette "Tastes Milder." Chairman Miller criticizes this case as one in which the consumer is in a position to judge whether the claim is true—presumably because it is one of taste.

The case is twenty four years old. It was made before the advent of low-tar cigarettes and the claim was prevelent for competing brands in the industry at the time. The consumer could not test the claim simply by smoking the advertiser's brand, but could instead be forced to try many brands making similar claims in order to make the comparison. Further, since the claim was perceived by consumers who read the ad to relate to physical irritation rather than taste, it is not solely a subjective judgment, and the final order was based in part on expert medical evidence that the claim could not be substantiated (though this case preceded the ad substantiation doctrine). It does not, therefore, help to establish Chairman Miller's claim that the FTC uses its resources to challenge claims that are simply matters of taste or opinion.

Gelb, 33 FTC 1450 (1941), aff'd. as modified, 144 F.2d 580 (2d Cir. 1944). The FTC challenged a hair coloring product manufacturer's claim that the effects of its product were permanent. Chairman Miller rightly states that the claim was too incredible to warrant Commission attention—but the case is forty one years old.

Sebrone Co., 34 FTC 1126 (1942), aff'd. 135 F.2d 676 (7th Cir. 1943). The Commission challenged a claim that the advertiser's brand of personal deodorant "kills strongest odors." The aroma of this case has certainly faded by now, it being forty years old.

Standard Oil Co. of California, 84 FTC 1401 (1974), modified 577 F.2d 653 (9th Cir. 1978). The FTC challenged a claim that a motor gasoline additive would cause the disappearance of virtually 100 percent of exhaust emission pollutants. Chairman Miller states that the Court of Appeals reversed this claim, stating "we do not think that any television viewer would have a level of credulity so primitive that he could expect to breathe fresh air if he stuck his head into a bag inflated by exhaust [as shown in the ad], no matter how clean it looked."

Chairman Miller's characterization of the case as one in which the FTC sought to protect the credulous falls apart if one reads the sentences that follow immediately after those he quotes: "If that were the whole case, we would agree with petitioners and overturn the Commission's order in its entirety. But the Commission's opinion made a different point. The Commission was concerned with the ads' implicit statements about the degree of reduction in auto emissions and the effect of that reduction on the auto pollution problem.

"Based on those principles and our review of the record, we find substantial evidence to support the Commission's finding that the three advertisements were misleading."

It is more difficult to make a case for amending the statute with respect to deception if quotes and charges are not taken out of context.

Trans World Accounts, Inc., 90 FTC 350 (1977), modified 94 FTC 141, further modified 94 FTC 1051, aff'd. in part and remanded in part 594 F.2d 212 (9th Cir. 1979). This case involved letters sent by a debt collection agency urging immediate payment of debts allegedly owed by the addressee, stating that failure to pay promptly "may result in commencement of litigation by our client." The FTC found the letters deceptive because they threatened imminent legal action that was not contemplated by the creditor. Chairman Miller states that the decision was in error, reading "may" to mean that legal action would result, not that it could possibly result, contrary to what the respondent had written in the letter. He says that the Court on appeal reversed the FTC's restrictions on the firm's use of the word "may".

In fact, the Court upheld the Commission's finding that use of the word "may" was deceptive. It said that legal action was not in fact contemplated by the creditor as a result of non-compliance with the letter request for payment, at least until an individual evaluation of the file had taken place. The concurring opinion characterized the collection letter series as "artfully phrased" to create an in terrorem effect on the alleged debtor.

While the Court did say that the FTC's *order* went too far in restricting the firm's future use of the word "may" in collection letters, that modification relates to the "fencing in" doctrine regarding the scope of orders meant to prevent further deception. It does not relate to the definition of "deception."

California Milk Advisory Board, 94 FTC 429 (1979). The FTC challenged ads claiming "everybody needs milk" because some people are allergic to it and others have an intolerance to it because they lack certain digestive enzymes needed to digest it. The Chairman states that the case was dismissed because the Administrative Law Judge found a lack of public interest in the proceeding, since the number of people allergic to milk was less than one percent.

Chairman Miller fails to note that the ALJ found the ad to be unfair and deceptive based on the ground that a significant portion of the population (including Asiatics and blacks) may have so-called "lactase deficiency." He found no public interest in entering the order, however. Chairman Miller's proposed definition of "deceptive" would not have affected the Commission's ability to sustain this charge in the complaint.

Jay Norris, 91 FTC 751 (1978), aff'd. as modified 598 F.2d 1244 (2d Cir. 1979). The FTC challenged a mail order firm's claim that a brand of men's socks offered for sale were "everlasting". Chairman Miller suggests this as another case in which the Commission used resources to protect the credulous.

However, the claim was not challenged or tried as literally true, but only as representing that the socks were of excellent durability and warranted by the manufacturer as to durability. The particular charge was dismissed not because the Administrative Law Judge found the claim was not deceptive, but because he found that the manner in which it was deceptive was not as charged in the complain and that it was not warranted to conform the complaint to the evidence at that point in the proceeding.

The claim was only one of several charged in the complaint, a number of which were subjected to a final cease and desist order. Neither was the case frivolous nor did the claim in question constitute the kind of legal challenge that Chairman Miller claims it did.

Bristol-Myers Co., 85 FTC 688 (1975). The FTC challenged claims for a personal deodorant as deceptive based on representations about the product's "dryness". It certainly was not a good use of Commission resources, but Chairman Miller fails to disclose that it was based on survey evidence establishing that the product characteristic in question was the one on which consumers made their purchasing decision.

This case is as close as Chairman Miller comes to a fairly recent misallocation of FTC resources in a deception case. But it stands virtually alone as evidence that there is a basis for defining deception by statute.

Firestone Tire and Rubber Co., 81 FTC 398, aff'd. 481 F.2d 246 (6th Cir. 1973). The FTC challenged use of the name "Safety Champion" for a tire, claiming that it implied the tire was safer than all other tires. The Administrative Law Judge enjoined use of the name dispite introduction of a survey showing only 1.4 percent of those who viewed the ad perceived it to make this claim. The Commission reversed the ALJ's order on this point.

Chariman Miller's analysis does not point out that this was only one charge in the complaint. The major charge, that the advertiser did not substantiate its claim that a line of its tires stopped "25 percent quicker", was upheld. The case involved, as well, other safety-related claims by the advertiser.

All this case shows is that the Administrative Law Judge made a bad decision on one claim in the complaint. Chairman Miller surely cannot establish that this case would have been brought on the single claim he picks out, nor does he question the rest of the case. Thus, there is no reason to believe that amending Section 5 to define deception would have had any impact on the FTC's allocation of resources.

Senator KASTEN. Thank you, Mr. Silbergeld. I would just like to remind all of the witnesses we have difficult time constraints this morning. I am trying to avoid using lights, buzzers, and bells to indicate that time is expired by having a polite system of notes. I would just please ask that all of you work within the constraints that we are trying to establish. We are doing everything we can to have balanced panels representing different kinds of opinions, but it is not going to work if we cannot stay within the basic groundrules.

Senator Packwood.

The CHAIRMAN. Mr. Connor, you would basically lump unfairness and deception together and use that tripartite standard?

Mr. CONNOR. Yes, Senator. A review particularly of the Commission's rulemakings tells us that they have done this; that the unfairness and deceptive concepts have not characteristically been distinguished by the Commission, and we ought to recognize this and treat them together.

The CHARIMAN. That would be substantial injury, unavoidable injury and a cost-benefit analysis.

Mr. CONNOR. That is correct.

The CHAIRMAN. Now, in the *Firestone Tire* case, where Firestone alleged that its tires would stop your car 25 percent quicker, would that case meet any of those tests at all? Is there any substantial injury to the consumer, for example, if they buy the Firestone tires and, indeed, they do not stop that quickly?

Mr. CONNOR. Well, I guess that is a factual question. On the face of it, I would think there would be.

The CHAIRMAN. You mean they really say to themselves, "Wow, these cars will stop 25 percent quicker, so I can extend my danger range a little bit and be able to get out"? Do you think they really think that?

Mr. CONNOR. I do not know, Senator.

The CHAIRMAN. I do not think so.

Mr. CONNOR. I cannot really answer that.

The CHAIRMAN. How would this case fit under your standard? Maybe it is unavoidable by the consumer—but you have to meet all three of these standards. Obviously, the consumer does not know if the Firestone Tire stops quicker than the Goodyear Tire. At least, they have no personal knowledge of it unless they go out and try out all kinds of different tires.

How do you, under that standard you are suggesting, stop that kind of advertising, or should you stop that kind of advertising?

Mr. CONNOR. I have not considered that specific case.

The CHAIRMAN. What you have is clearly misleading advertising with no facts to justify the conclusion.

Mr. CONNOR. Yes.

The CHAIRMAN. But where is the substantial injury to the consumer that is unavoidable by the consumer and not outweighed by conterveiling benefits? It seems to me that under your standard, deceptive advertising is just going to go right on, and there is no standard by which you could stop it.

Mr. CONNOR. Well, we start—you start—the first question I think you asked is whether this is—is the underlying truth or falsity of the statement. One thing we do not want to put ourselves in the position of is appearing to advocate deliberate falsehood or reckless disregard for truth. If in fact the statement is on the ground that there is no—

The CHAIRMAN. In the *Firestone* case, you did not have any evidence that the tire stopped that much quicker. They had the chance to prove that and they simply could not. You may say it is not deliberate; it borders on reckless. Why not say 30 percent, 50 percent? There was no evidence that they would stop that much quicker.

Mr. CONNOR. Yes.

The CHAIRMAN. Either you are saying well, that kind of advertising is all right. It is free play of marketplace ideas, and that nobody really is going to drive their car that much faster on a slick pavement, no matter what the ads say, and there is no substantial injury to any particular consumer. In the aggregate you might have millions or billions spent on Firestone Tires, but for any individual consumer, no injury—just let them go on with the advertising.

Mr. CONNOR. What we say in our prepared statement, Senator, is that we are not attempting to disturb the common law notions of deception that if a statement is false or if it was made with a reckless disregard for the truth, we have said we regard this as a form of per se injury to the consumer.

The CHAIRMAN. And the consumer could bring a suit.

Mr. CONNOR. It would be actionable by the FTC.

The CHAIRMAN. Where is it actionable under the three standards of substantial injury, unavoidable, and cost-benefit?

Mr. CONNOR. Our assumption is that there is substantial injury, that there is injury if the statement is false or if it—we have wrestled with this, Senator, and if our words do not adequately express this—

The CHAIRMAN. I want to make sure what you are saying here. If the statement is false, that will presume substantial injury, then?

Mr. CONNOR. If the statement—well, I think the common law would say if the statement was known to be false or was spoken with reckless disregard——

The CHAIRMAN. All right.

Mr. CONNOR [continuing]. Then we would say there is consumer injury there.

The CHAIRMAN. And you can say that without having to prove the injury in that case. The statement in and of itself makes the injury appear.

Mr. CONNOR. That is right. We have been concerned whether our—the language we are proposing actually meshes with the position we have taken in our statement to that effect, and would work with the staff if it does not.

The CHAIRMAN. Well, if you are willing to say that the FTC can bring these actions so long as they can prove that the statement was made recklessly or without any knowledge of the truth, then that indeed is all the injury that has to be proved.

Mr. CONNOR. That is certainly our intention.

The CHAIRMAN. That is good, I am glad to hear that. Thank you. I might be able to live with in that case. I have no other questions, Mr. Chairman.

Senator KASTEN. Senator Ford.

Senator FORD. I want to see if I can live with it, Bob.

Mr. Connor, since you have been in the forefront, let us just keep it that way. I will ask you a couple more questions. If deceptive acts or practices are not defined in reauthorization legislation, would the chamber support a provision to eliminate unfairness as a basis for rulemaking in the commercial advertising area, section 18?

Mr. CONNOR. Yes, Senator, we would. We have stated our preferred position here, but failing that——

Senator FORD. How about the elimination of unfairness as a basis for case-by-case adjudication under section 5?

Mr. CONNOR. Simply eliminating?

Senator FORD. In commercial advertising cases?

Mr. CONNOR. We have not addressed that question, Senator. I mean we have simply approached the question from a different direction. I am not——

Senator FORD. Apparently Senator Packwood is coming from a different direction.

Mr. CONNOR. You see, the underlying problem I think we have, as I expressed in my remarks, is a difficulty in distinguishing unfairness and deception.

Senator FORD. Let me ask you this. My understanding, and not being a lawyer it is very tough dealing with lawyers, but it is my understanding that the courts have not defined unfairness. They have defined, deception.

Mr. CONNOR. That is generally correct I think.

Senator FORD. Then you just want to lump unfairness and deception together and go on the basis of the courts' deception standards.

Mr. CONNOR. Senator, if, you know, failing the solution that we are proposing, I would have to say that I suppose I would agree with what you are suggesting, but we do have reservations that that is an adequate solution which is why we have made the proposal we have.

Senator FORD. Let me ask Mr. Montgomery a question then. You say on the second page, the last paragraph of your statement. In contrast to the FTC Act, these State statutes are enforced almost exclusively through recourse to State judicial systems rather than through an administrative agency proceeding.

There is a feeling that this is where most of these cases ought to go. Do you have any comment as it relates to what you are saying about the statutes of the States?

Mr. MONTGOMERY. I am not expressing any view on the appropriateness of——

Senator FORD. Are you saying the state statutes are primarily construed in State courts and not by the Commission?

Mr. MONTGOMERY. That is right, Senator. State legislatures have made a decision that we do not have the bureaucratic resources to function on an administrative agency basis. Were we administrative agencies, we might be required to regulate the marketplace in a fashion that State attorneys general do not ordinarily do. We are law enforcement officials, we make individual case selections and we bring them to the courts. We do not make decisions as to what is unfair or deceptive; we ask the courts to do that.

Senator GORTON. Senator Ford, having been in that business myself, I can assure you that it is almost universally the case. The State attorney general consumer protection activity does not ordinarily or in any instances of which I know deal with rulemaking. It is case by case and court interpretation.

Senator FORD. Let me ask this question, and if you want to get in this colloquy, Senator, it would be fine, and I hope I do not run over my time.

Where should the State licensing boards and the FTC stop?

But where should the State's jurisdiction stop and the FTC take over? Or should there be a line drawn between the two?

Mr. MONTGOMERY. I think there needs to be a line. You are asking a difficult marketplace question.

Senator FORD. We are getting into a difficult area.

Mr. MONTGOMERY. My understanding is the FTC, Senator—with the exception of the eyeglass rule, has not made an effort to override the licensing and regulatory decisions of state agencies in most cases. They have not done that. That is a very difficult line and one that we in the States are very sensitive to.

On the other hand, the FTC has a very unique perspective, a national perspective on how the marketplace operates. To the extent that they have developed a viewpoint expressed in reports which criticize and point up some deficiencies in the operation of State licensing systems, to the extent that they restrict access to the market, I think that that is a very appropriate role for a national agency to play.

Senator FORD. We heard testimony yesterday that purely intrastate advertising should not be regulated.

Mr. MONTGOMERY. Actually, Senator, in my experience, the FTC really has not been involved, at least in the northeast States, in matters which affect only one State; they usually do provide a very unique interstate perspective on the problems that we have, and that is why we have found working with the regional offices so helpful.

Senator KASTEN. Do you have one more question, or several more?

Senator FORD. I have several more.

Senator KASTEN. Senator Gorton.

Senator GORTON. Mr. Connor, I would like to go back to the same general subject matter that Senator Packwood covered. As a representative of the chamber of commerce, was your drafting of these three sets of conditions including the precondition of substantial economic injury to consumers, consciously designed to remove entirely from the jurisdiction of the Federal Trade Commission or, for that matter from the courts, the impact of unfair and deceptive practices on competitors?

Mr. CONNOR. No, no, Senator. The language which we have adopted here is, of course, the language of the commission's own

1980 policy statement. We were *directing our attention in this proposal* only to the question of protecting the consumer.

The earlier provision dealing with unfair methods of competition which we have not discussed in this hearing deals with the protection of the competitive process.

Senator GORTON. So you want to limit the jurisdiction of the Federal Trade Commission in protecting consumers, but not competitive business enterprises.

Mr. CONNOR. I think that is protected by another provision of section 5, Senator.

Senator GORTON. You are not asking for any limitation on the Federal Trade Commission's jurisdiction in that respect?

Mr. CONNOR. I do not believe the provision we are discussing has been read as a competition—has been used by the Commission as a competition statute. We are not attempting to limit them in any way.

Senator GORTON. That is what my question was. You only wish to limit the Federal Trade Commission's powers in respect to the protection of consumers, not to limit its powers in respect to the protection from unfair competition.

Mr. CONNOR. In the discussion we have had here today, that is correct. Our written statement contains suggestions with respect to the provisions on unfair methods of competition. But we were advised by the chairman that he did not want that subject discussed here.

Senator GORTON. A question, then, for Mr. Silbergeld and Mr. Montgomery, either or both. My impression is that during the course of the last 2 or 3 years at least, you have long since abandoned draining the swamp while you swat away at alligators, and that you have a whole lot of alligators as far as you are concerned in the proposals that have been made by Chairman Miller, by the chamber and by others.

If you are willing to do so at this point, I would like you to give me a brief outline of what you consider to be the most damaging of these proposed changes, and those which, while you do not particularly like them, you do not think will substantially undermine consumer protection.

Mr. SILBERGELD. Yes, Senator. I would give approximately equal weight to any changes in the statutory—any statutory definitions of the term deception in section 5, and to the exemption of the professions, although I think that a State action kind of limitation that already applies to the Justice Department antitrust cases would be acceptable.

Less important but also of concern is the question of codifying the standards for unfairness simply because we believe it will result in a tremendous amount of litigation. But I think I could probably send up some language that might satisfy both the desire to codify and the desire not to make litigation unduly extensive over the codification.

Senator GORTON. Mr. Montgomery, does that express your views as well?

Mr. MONTGOMERY. Yes. Deception is our primary concern. We do not think that it is appropriate at all to limit deception. In particular, we are concerned with the chairman's proposal to analyze the reasonableness of consumer conduct to create distinctions between reasonable and unreasonable and vulnerable and gullible consumers. We think that is extremely dangerous.

Senator GORTON. Finally, Mr. Montgomery, a question for you. You have expressed concern with the impact of statutory changes on State enforcement activities and State court activities, obviously because most State statutes either include the instruction to parallel Federal court decisions in their interpretation or State courts have followed Federal court decisions voluntarily.

Do you really think that if there were substantial changes in the Federal statute which did not cause similar changes on the part of State legislatures, that State court interpretations of State law would become more restrictive?

Mr. MONTGOMERY. I am very concerned that that would be the case, Senator. I certainly cannot state as a matter of fact that it would occur. I do not think it would occur at all next year. Perhaps not the year after. But the State courts very much depend upon the developed experience and the wealth of jurisprudence under the Federal Trade Commission Act; and I think as that jurisprudence changes, and changes radically under Chairman Miller's proposals if they are adopted by the Congress, that you are going to see States following suit.

Senator GORTON. Thank you, Mr. Chairman.

Senator KASTEN. Senator Exon?

Senator EXON. Mr. Chairman, thank you very much. I join my colleagues in welcoming you gentlemen here to express the positions of the organizations that you ably represent. I would like to go into a matter—if it has been covered before I previously got here, then I apologize for being late. But if not, I would direct my basic question to the gentleman from Massachusetts, Mr. Montgomery, who I believe is chief of the consumer protection division in Massachusetts.

During the years when I was Governor of Nebraska, our consumer protection division was embodied with the attorney general, also. Was that true in the State of Washington? If I could have the attention of my colleague from Washington, the consumer affairs division, was that a part of the attorney general's office in the State of Washington?

Senator GORTON. Yes, it was, and I was attorney general, and that is the reason I know something about it.

Senator EXON. Likewise in Nebraska. And I assume that is the case in Massachusetts.

Mr. MONTGOMERY. Yes, Senator.

Senator GORTON. It is not universally the case, but it is by far the most common.

Senator EXON. OK. My question was how many States incorporate their consumer protection laws divisions enforcement in the attorney general's office and the attorney general is the chief law enforcer, other than the Governor, and how many do not?

Mr. MONTGOMERY. Senator, my analysis of the State statutes shows that while some States separate the litigation function from investigation, consumer complaints and that sort of thing performed by a separate executive agency, that all 50 States, under statutes which are patterned primarily after the FTC act, authorize the attorney general, and exclusively the attorney general, to bring actions in State courts to protect consumers from unfair deceptive practices.

Senator EXON. How many States did you say?

Mr. MONTGOMERY. Fifty. And I have attached to my testimony——

Senator EXON. All 50?

Mr. MONTGOMERY. Yes. I have attached to my testimony a compilation of all 50 State laws.

Senator GORTON. But it would be more like 40 to 45 States in which the run-of-the-mill complaint goes through the attorney general's office.

Mr. MONTGOMERY. That is right.

Senator EXON. It has always been a concern of mine that however well intended—and I think the Federal Trade Commission has done yeoman work in many, many areas and that is why I have always taken a position that I am not in favor of eliminating the Federal Trade Commission. But I still feel that there are many areas where I think they have gone far, far afield beyond the intent of the legislation, and we always get into that when we delegate authority to the various agencies, generally referred to as the bureaucracy of the Federal Government.

And I was just wondering if you have not commented on it, how—what would your perception, Mr. Montgomery, of following the lead of the States in this matter, rather than the lead of the Federal Government, and give more and more of the filing of lawsuit authority to the Justice Department of the U.S. Government pursuant to the general flow of the responsibility in the States?

Mr. MONTGOMERY. Well, in essence, I assume, Senator, you are talking about really transforming the FTC from an administrative agency into a prosecutorial agency. And I am not really in a position to answer the question because it involves substantial questions concerning the allocation of Federal resources. Is the agency capable of handling that kind of a burden? Are the Federal courts capable of handling it? And I do not know the answer to those questions. I certainly cannot say that we have been unhappy at the State level with our experience in prosecuting our actions in State court. But we also, I think, are somewhat limited in the number of cases we can bring, and in perhaps the consistency of approach that we can expect from State court judges.

If I could just make another comment. We do understand at the State level that there have been some criticisms of the performance of the Federal Trade Commission, particularly as Mr. Connor has said, in the area of rulemaking. What concerns us most today is that the committee is not talking about just restricting the agency's rulemaking authority or even their jurisdiction in the area of case-by-case adjudication. We are talking about changing the standards of conduct by which we judge whether businesses are treating consumers in an appropriate manner. That is what concerns us the most.

We do not think that that is appropriate at all, and we think it will have a spinoff effect on the behavior of marginal and fly-by-night businesses that we are fairly successful at handling these days. And in addition, it may very well effect, as I think Senator Packwood was suggesting, the Firestone-type advertising.

Senator EXON. Are there any comments from the other members of this panel? That is the only basic question I have on the point that I have raised. Yes?

Mr. SILBERGELD. Senator, I think what you would find would be a great reduction in the number of clearly justifiable FTC cases prosecuted, simply because the Justice Department would then have to trade off the resources that they use for those cases against resources for cases in all sorts of other areas unrelated to trade regulation. And I do not see that the number of cases that the FTC is or should be bringing is so miniscule that there is no justification for their continuing to use the administrative process to do that.

Their decisions are subject to judicial review, of course, and any final order is appealable to the U.S. courts of appeal.

Senator EXON. My time has expired. Let me just say this in response to your question, one back. Is it not true, though, that if we have to keep some businesses and businessmen in line, because I think we should recognize that every people—every person male or female who is in business is not necessarily a saint. And I think therefore we do have to have some laws to help keep them in line.

Is it not true, though, that business in general, if there is the threat of a lawsuit brought by the Justice Department, isn't that threat hanging over their head somewhat of a deterrent to any wholesale abuse of what is intended in the act? Or putting it another way, certainly at the present time the Federal Trade Commission is not prosecuting each and every instance that could or should be a violation of the intent of the act.

What I am trying to say, if we could eliminate all of these court actions that are going on, and if it were properly handled and enforced on a selective but detailed basis by the Justice Department, would that not likely send a signal out that if you get out of line, you are very apt to be hit pretty hard by the Justice Department?

Mr. SILBERGELD. Well first of all, I guess I just do not agree with the premise that the Justice Department will give priority to those cases, Senator. And second, I think that what the Commission does now sends signals. The problem is that some members of the business community do not like some of the signals that are being sent, and that really is the debate. Not, I think, the question of whether prosecution in the Federal courts or administrative proceedings are more of a deterrent.

In fact, I think most business people will tell you the biggest deterrent is not the question of who is going to prosecute the case or in what forum, but the question of publicity regarding the case. And it is publicity that is the deterrent from the business point of view, regardless of who the prosecutor is.

Senator EXON. In Nebraska, if the attorney general filed an action, it would get a lot more publicity than if it were filed by one of the bureaucratic agencies. But I thank you for your input. It has been helpful. Thank you, Mr. Chairman.

Senator KASTEN. Mr. Montgomery, do you share the view that was expressed by Mr. Silbergeld, that it may be appropriate to apply the State action doctrine to FTC antitrust cases?

Mr. MONTGOMERY. Yes.

Senator **Kasten**. If I understand correctly, the bill that Senator Cannon has introduced would make the State action doctrine apply.

Senator **Ford**. Nose to nose.

Senator **Kasten**. Senator Packwood, do you have further questions?

The **Chairman**. No questions.

Senator **Kasten**. Senator Ford, do you have further questions?

Senator **Ford**. I have one or two, Mr. Chairman. This is my best side right here.

Mr. DeLong, let me ask you this question. You gave some interesting statements in the beginning. Should the FTC retain authority to include affirmative rules of conduct in trade regulation rules?

Mr. **DeLong**. You mean, aside from simply forbidding the practice that is found to be unfair or deceptive?

Senator **Ford**. Yes.

Mr. **DeLong**. I would say yes, but this is certainly an area that has caused profound problems for the agency and, I might add, for everybody else. Again, I would like to go back into the history for just a minute. The problem has always been that some people in the agency have tended to regard finding the existence of unfair or deceptive practices as a kind of jurisdictional trigger. Once you find "enough," then that entitles you to do almost anything you want to anyone in the industry, whether they have been engaged in the practice or not, and to do so on what is called the fencing-in standard, which is derived from litigation and which means the FTC can "close all routes to the prohibited goal." So what you wind up with is an assertion of unlimited authority to do anything to anyone even if he has not engaged in the practice, regardless of cost.

Senator **Ford**. That is a very interesting statement. I hope the Senators on this committee would pay attention to what you have just said. Obviously, you have some insight and experience that is very valuable.

Mr. **DeLong**. There was another part of the FTC that said that what you had to do on remedies was, essentially, to apply a cost-benefit test, and look at the damage being caused by the practice against the harm that might be caused by the remedy.

Obviously, that is the wing to which I belonged.

It seems to me the remedies question is well worth addressing and needs to be addressed in a cost-benefit context.

Senator **Ford**. This might be addressed to the panel. The chamber of commerce has proposed legislation to define unfair methods of competition to be limited to the Sherman and Clayton Acts. Senator Cannon has introduced a bill—I do not know whether you have had an opportunity to see it yet or not—which endorses the FTC's current antitrust mission, and is formulated to allow the Commission to bring cases involving conduct that is not inconsistent with the Sherman or Clayton Acts. Could I have any kind of reaction to these proposals? Mr. Connor.

Mr. **Connor**. Senator, maybe I should start, since you began by describing the chamber's proposal.

Senator **Ford**. I hope I was right.

Mr. **Connor**. Let me begin by just saying a word about what it is that the chamber has proposed. What the chamber is trying to do is not to reduce or minimize in any way the FTC's antitrust authority. What we are attempting to do is restrict their jurisdiction under unfair methods of competition to antitrust matters. We are attempting to have the statute say that this is an antitrust statute, and it is not intended to pursue social or sociopolitical goals.

The proposal does not say simply that unfair methods of competition are to be equated with the Sherman Act or Clayton Act violations. There are two steps. It says that, but then it also says that an unfair method of competition includes anything which Congress defines to be an unfair method of competition. And we felt that was very important.

What we are saying is that if the Commission thinks it finds one of these famous interstices in the antitrust laws, and it thinks it should step in and declare this, although not a violation of the antitrust laws, to be a violation of the FTC Act, it should come up to this committee and ask this committee to agree with it, and have that particular conduct defined to be an unfair method of competition by the Congress, instead of going through years of litigation ending in the courts and with legislative veto and all this sort of thing.

The proposal in Senator Cannon's bill is one that the Chamber Antitrust Policy Council has not looked at. So anything I say on that is just my own view. My initial reaction was that it is obviously targeted at the same thing the chamber's proposal is, to say clearly that unfair methods of competition means antitrust.

As I have thought about it since first seeing it a few days ago, I have begun to wonder, however, begun to worry whether principles not inconsistent with the antitrust laws are any more clear or definite than unfair methods of competition, and I am beginning to be afraid that we would have just as much confusion and chaos arguing about what the principles underlying the Sherman and Clayton Acts are as we have today in discussing unfair methods of competition.

Senator **Ford**. Would anybody else on the panel wish to respond to that question?

Mr. **Silbergeld**. Senator, just one point. I do not think it is accurate to say that the unfair methods of competition standard is simply a matter of antitrust. From 1914 until 1938, when the Wheeler-Lea amendment to section 5 was passed, it included deception as an unfair method of competition because deceiving the public into buying your product was taking sales away from competitors, and even though that may have been cured by the Wheeler-Lea amendment, which clarifies that that kind of practice is now unlawful because it harms consumers, there are such practices as appropriation of others' trade names and use of names deceptively similar to those of a competitor, and all sorts of other things that may not be strictly a violation of the antitrust laws.

That may well have long historical and jurisprudential definition of unfair methods of competition. I think you would want to see a very extensive analysis of what any change or bounding of the term "unfair methods of competition" would do to the long list of practices that are used by one competitor against another, where you would want to change it.

Mr. **DeLong**. Could I add one word to that? I do not think the idea has ever been rejected, has it? In Senator Packwood's Firestone example, it would still be an unfair method of competition to deceive consumers into buying your product rather than an equally good one made by a competitor.

Mr. **Montgomery**. If I could add just one comment for the record, I am here only representing the Consumer Protection Subcommittee of the National Association of Attorneys General, and I have not studied these antitrust proposals, but I think it is fair to say, I am sure that the association would be opposed to any restriction in the antitrust authority of the Federal Trade Commission.

Senator **Ford**. If they would be opposed to any change in the antitrust authority——

Mr. **Montgomery**. We would be concerned with any change which restricts the definition of unfair methods of competition in the Federal Trade Commission Act because of its effect on Federal antitrust policy as well as its effect on State antitrust enforcement, because many of our State statutes also contain the phrase unfair methods of competition. We would be concerned that either as a result of legislative action or as a matter of interpretation by State court judges, we would find the same restrictions being put into our State statutes.

Senator **Ford**. You lawyers straighten me out a little bit. I have always heard that unfairness is in the eye of the beholder. I do not know of many cases that have been brought by the FTC that they have won solely on unfairness. Of course, now we are talking about antitrust.

Mr. **Silbergeld**. Well, unfairness has not been definitively and completely defined by the courts, partly because the concept does not come out of a long history of jurisprudence that precedes the original FTC Act of 1914. The *S. & H.* case certainly contains an attempt to define elements that were used to measure deception, Senator, but as the 1980 letter to you and Senator Danforth points out, even that concept, the Commission has found to be not completely useful.

They have, for instance—they state that they have abandoned one of the three elements identified in *S. & H.*, the element of whether the practice is immoral, unethical, et cetera, et cetera, because it is duplicative of the injury question. They say, you know, almost every case the Commission has brought using an unfairness theory in whole or in part, that anything that is immoral or unethical or anything else on that list that constitutes that third element in the *S. & H.* case, it always injures consumers. So it is an unnecessary inquiry, once you have established injury, to go back and again look at the ethical nature of the practice or the morality of the practice.

So, I would say that the courts have taken a look at what can be used to establish unfairness in particular cases, but they have not provided anything that would serve finally as a statutory definition.

Senator **Ford**. My time is up, Mr. Chairman. I might make a suggestion to the chairman that we try to get views from several quarters on unfair methods of competition, and see what we can come up with. It might be helpful. Thank you.

Senator **Kasten**. Senator Gorton.

Senator **Gorton**. No further questions.

Senator **Kasten**. Senator Exon.

Senator **Exon**. No further questions.

Senator **Kasten**. Senator Packwood.

The **Chairman**. No further questions.

Senator **Kasten**. On behalf of the committee, I would like to thank the four of you for your very helpful and informative testimony.

Our next panel includes Mr. Rogal, Mr. Weil, Mr. Versfelt, Mr. Greenberg, and Mr. Pepples.

The committee will come to order.

Our first witness will be Mr. William Rogal, who represents the American Advertising Federation, and who will be speaking as well for the Association of National Advertisers and the American Assoication of Advertising Agencies. I understand that you are joined by Mr. Gilbert Weil and Mr. David Versfelt. I greatly appreciate the fact that you were able to combine your testimony, and that Mr. Weil and Mr. Versfelt are here to respond to questions from the committee.

Mr. William Rogal.

STATEMENTS OF WILLIAM W. ROGAL, AMERICAN ADVERTISING FEDERATION; ACCOMPANIED BY GILBERT WEIL, ASSOCIATION OF NATIONAL ADVERTISERS; AND DAVID VERSFELT, AMERICAN ASSOCIATION OF ADVERTISING AGENCIES; AND DAVID I. GREENBERG, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA, AND ERNEST PEPPLES, BROWN & WILLIAMSON TOBACCO CORP.

Mr. **Rogal**. Thank you, Mr. Chairman.

As stated, this is a joint statement of the three principal advertising associations. Before we propose and explain our amendment, it is important that we point out some of the things that we are not trying to do.

In the first place, we are not seeking to shield advertisers who might disseminate advertisements which are false, deceptive, or misleading from prompt and effective prosecution by the Federal Trade Commission. However, we agree with Chairman Miller's view that the FTC has been overzealous at times in its application of its deception powers, and we appreciate his efforts to develop legislative language to clarify the scope of those powers.

Chairman Miller's receptivity and willingness to work closely with this committee and the Congress in the development of reform legislation presents a rare opportunity to improve FTC procedures significantly. We have not had the time to fully explore the implications of his proposal in regard to deception. It is a proposal worth careful examination, and we request the opportunity to submit supplemental comments when we have completed our analysis.

Senator **Kasten**. Without objection, you will be permitted to do so.

Mr. **Rogal**. Second, it is not our intention to affect in any way the FTC's power to require that positive claims made in advertise-heaped upon advertising by the Commission in the 1970's, such as in the area of children's television advertising, over-the-counter drugs, games of chance in the food retailing and gasoline industries. In each of these industries, truthful advertising devoid of deception would have been and has been suppressed.

At this juncture, the logical question arises, if the abuses have been mainly confined to the rulemaking area, wouldn't it be adequate to make permanent the present temporary ban on the use of unfairness in rulemaking, or stated another way, why does the advertising community feel that it needs protection in the case-by-case area?

The short answer to these questions is that any act or practice the Commission can regulate in rulemaking, it can regulate in case-by-case adjudications. If unfairness remains for advertising adjudications, the Commission might decide to bring individual cases against advertisers based on the same unfairness theories which produced the aborted over-the-counter drugs and children's television rules.

The threat of a possible unfairness charge operates as an effective chilling prior restraint on inventiveness and innovation. Advertising is an art form. It must motivate and persuade or its cost constitutes an economic waste. Advertising must have freedom and elbow room to do its legitimate job, and our proposal does no more than preserve the liberty which advertisers enjoyed until the Commission's recent unfairness initiative.

The committee should also think about the tremendous economic costs which many of these proceedings, even though aborted, placed upon both the public sector and upon private advertisers.

I believe I will leave our constitutional argument stand as it is in our full statement, in the interest of time. I would like to move on.

We are well aware that in its letter of November 13, 1979, to Senator Ford, the FTC's Commissioners charged that excision of their alleged authority to regulate speech on the ground of unfairness would adversely affect their ability to protect children from physical dangers created by advertising. In support of this argument, they refer to several consent orders to cease and desist which are ostensibly based upon the unfairness theory.

These consent orders interdicted advertisements which depicted youthful models carelessly riding bicycles on busy streets, depicted a naturalist eating unidentified wild plants, and depicted a child cooking rice on a gas stove. I believe there was another case which depicted a child using a hair dryer to dry its doll's hair in close proximity to a sink full of water.

These cases were not litigated, and therefore do not demonstrate that the Commission would have been powerless to challenge the advertisements even if the word "unfair" were not in its statute.

Indeed, classic principles of deceptiveness should be adequate to cover any advertisement that falsely misleads children to do something dangerous.

I might point out that I reviewed the cases recently, and in each of the complaints the activities or the advertisements are charged as having constituted unfair methods of competition and unfair or deceptive acts or practices, and in each of the complaints there is a ments must be substantiated by and based upon factual support in the possession of the advertiser, such as would satisfy the reasonably prudent advertiser as to their truths.

First, it is our view that the Federal Trade Commission should not have the power to proscribe or restrict truthful, nondeceptive, commercial speech under the unfairness doctrine. Our primary aim is to secure legislation which will protect commercial speech from the types of abuses it has been subjected to by the FTC over the past 10 years.

Specifically, we are asking this committee to prepare legislation which will provide that commercial speech or advertising shall be henceforth regulated by the Commission only under the more than adequate deception standard, rather than the amorphous unfairness doctrine. More specifically, it is our proposal that advertising as a form of constitutionally protected speech should be specifically exempted from application of the unfairness standard.

If advertising is to continue to play its vital role in our economy, it must be kept free from unjustified prior restraints. Truth and accuracy are concepts which advertisers can and should live with.

On the other hand, advertising cannot live with the amorphous and ever-changing concept of unfairness which, as Senator Ford states, like beauty, varies with the eye of the beholder. We understand that other groups are seeking a blanket exemption from FTC jurisdiction. This is the farthest thing from our minds. The Federal Trade Commission must continue to have jurisdiction to police our industry, to make certain that advertising content is truthful, honest, and devoid of deception.

Here is our proposal. We propose that the Federal Trade Commission Act, sections 5 and 18, be permanently amended to provide that the term "unfair acts or practices" does not apply to commercial speech.

We have two basic reasons for recognizing this constitutionally dictated protection for commercial advertising. The first reason is that it is needed, absolutely needed to preclude the types of abuses which have taken place in the past. The second reason, obviously, is that advertising, unlike most other acts or practices, within the FTC's jurisdiction, is a form of speech protected by the first amendment.

First, as to the need for the legislation, in 1979, this committee's report on S. 1991 explained the reason for denying the FTC funds to initiate any new rulemaking against advertising based on the unfairness doctrine by stating that the Commission has used its rulemaking power to, and now I am quoting from the report, "initiate proceedings in which the unfairness doctrine has been used a a broad charter for restricting commercial advertising solely because it may have consequences that the Commission finds objectionable or is otherwise contrary to the Commission's concept of fairness."

The committee further explained that the legislation was intended to redirect the Commission to its primary and long-standing function of determining whether advertising contains representations that are false or have the capacity to deceive or mislead consumers.

In our filed full statement, we present several examples of the type of abuse that this committee is well aware of that were separate paragraph stating that the advertiser was in competition with others in the sale of similar goods.

I would like to now address the other main thrust of our efforts here. We believe and strongly urge that section 5(M)(1)(b) of the Federal Trade Commission Act should be repealed. The reasons are set out quite fully in our statement. We consider that this provision constitutes back-door rulemaking. It hangs like a sword of Damocles over the heads of all advertisers. The Commission's chilling use of it and apparent intent to wield it is evident in its widespread in terrorem circulation of existing cease and desist orders to the industries involved with its unmistakable implications.

We are concerned that that section affords the Commission the way to select some smaller complacent company as a target, exact from it a consent or weakly litigated order to cease and desist, and then enforce the order against an entire industry. This is not the way industrywide rules should be promulgated, for it makes a mockery of the due process rights of advertisers and other businessmen.

Thank you. That completes my statement.

[The statement follows:]

STATEMENT OF THE AMERICAN ADVERTISING FEDERATION, THE AMERICAN ASSOCIATION OF ADVERTISING AGENCIES, AND THE ASSOCIATION OF NATIONAL ADVERTISERS

This statement is respectfully submitted jointly by the American Advertising Federation (AAF), the American Association of Advertising Agencies, Inc. (AAAA) and the Association of National Advertisers, Inc. (ANA), national trade associations which together represent the overwhelming majority of all persons and companies which comprise the advertising industry in America. Our principal purpose in submitting this statement is to propose amendments to the Federal Trade Commission Act which will prevent future abuses by the FTC of its authority to proscribe or regulate commercial speech.

IDENTIFICATION OF THE ASSOCIATIONS

The AAF is a national trade association which includes within its membership all of the various elements of the advertising industry. Its principal office is located at 1225 Connecticut Avenue, Northwest, Washington, D.C. 20036. The membership of the AAF includes companies which manufacture and sell consumer products, advertising agencies, newspaper and magazine publishers, radio and television broadcasters and networks and approximately 22 other trade associations with memberships composed of companies engaged in various advertising pursuits. The Federation also represents the "grassroots" of the advertising industry because it is the parent body of more than 200 local advertising clubs and federations located throughout the United States and having a combined membership of approximately 25,000 advertising practitioners. These local organizations, like the parent body, include advertisers, advertising agencies and media within their membership.

The AAAA is the national association of the advertising agency business. Its more than 540 members, both large and small, are located throughout the United States and handle approximately 75 percent of all national advertising placed by advertising agencies in this country. Its address is 666 Third Avenue, New York, New York 10017 and it maintains a Washington office at 1899 L Street, Northwest, Washington, D.C. 20036.

ANA is a not-for-profit corporate trade association, organized and existing under the laws of the State of New York with offices at 155 East 44th Street, New York, New York 10017. It is composed of approximately 400 companies located throughout the United States which manufacture and sell a wide range of products and which employ advertising as an important element of their marketing and public relations programs. Although ANA's membership includes many of the nation's largest advertisers, it also includes a large number of smaller ones. Approximately one-third of ANA members spend under $1 million annually for advertising. The common characteristic of all ANA members is that they purchase space and time from the media of mass communications.

INTRODUCTION

Before we propose and explain our amendments it is important that we point out some of the things we are not trying to accomplish.

In the first place we are not seeking to shield advertisers who might disseminate advertisements which are false deceptive or misleading from prompt and effective presecution by the FTC. We recognize that the FTC has on occasion been overzealous in enforcing its power to enjoin "deceptive" advertising but we prefer to leave the final word on the concept of deception with the courts, where it now lies. In our view material deception, i.e., claims or statements having the capacity to deceive consumers, cannot be countenanced in our industry under any circumstances.

Secondly, it is not our intention to affect in any way the FTC's power to require that positive claims made in advertisments must be substantiated by and based upon factual support in the possession of the advertiser such as would satisfy a reasonably prudent advertiser as to their truth. We believe that such positive claims as "get 14 percent better performance" or "9 out of 10 people prefer" clearly represents to the consumer that the advertiser has conducted tests or surveys or has some other basis for making the statements in good faith. The implication is false, i.e., "deceptive", if the advertiser in fact lacks such material.

These three associations, together with the Council of Better Business Bureaus, Inc., jointly established and sponsor the National Advertising Division and the National Advertising Review Board. This self-regulatory mechanism, now in its eleventh year, is, without question, one of the most active and effective self-regulatory bodies ever devised. Several chairmen and commissioners of the Federal Trade Commission have highly praised its work and have publicly asserted that the NARB, by promptly and efficiently correcting advertising abuses has "taken the heat" off the Commission and permitted it to expend its efforts elsewhere, except where necessary to add teeth to the NARB's operation.

Finally, we are not seeking to destroy or weaken the FTC in any way. Insofar as advertising is concerned we believe that a national regulatory body is needed and is far preferable to the alternative of having each of the 50 states issuing conflicting regulations as to how interstate advertising must be conducted. But, our industry is acutely aware that the FTC has, in the recent past, overstepped the boundaries of its congressional mandate and we turn now to our specific proposals for legislation to prevent a recurrence of such overstepping.

THE FEDERAL TRADE COMMISSION SHOULD NOT HAVE THE POWER TO PROSCRIBE OR RESTRICT TRUTHFUL, NONDECEPTIVE COMMERCIAL SPEECH

As stated earlier, our primary aim is to secure legislation which will protect commercial speech from the types of abuses it has been subjected to by the FTC over the past 10 years. Specifically we are asking this Committee to prepare legislation which will provide that commercial speech or advertising shall be henceforth regulated by the Commission only under the more than adequate deception standard rather than the amorphous unfairness doctrine. More specifically it is our proposal that advertising, as a form of constitutionally protected speech, should be specifically exempted from application of the unfairness standard.

If advertising is to continue to play its vital role in our economy it must be kept free from unjustified prior restraints. Truth and accuracy are concepts which advertisers can and should live with. They have, over the years, developed the ability to refrain from disseminating advertisements which have the "capacity to deceive" and are guided in that effort by 67 years of precedent. On the other hand, advertising cannot live with the amorphous and ever changing concept of "unfairness". The concept is not a standard in the usual sense of the word for it, like beauty, varies with the eye of the beholder.

Before giving the specifics of the proposal we wish to emphatically make it clear that we are not seeking any diminution of the Commission's power to proceed against deceptive advertising. We understand that other groups are seeking a blanket exemption from FTC jurisdiction. This is the farthest thing from our minds. The FTC must continue to have jurisdiction to police our industry, to make certain that advertising content is truthful, honest and devoid of deception.

Our aims today are the same as our aims which were expressed to this Committee in various filings and statements when the FTC Improvements Act of 1981 was under consideration. As you know we were partially successful at that time in that the Congress enacted section 11(b) of that Act which prohibited the Commission from expending any funds for fiscal years 1980, 1981 and 1982 for the purpose of initiating any new rulemaking proceedings which would prohibit or regulate "commercial advertising on the basis of a determination by the Commission that such commercial advertising constitutes an unfair act or practice in or effecting commerce."

Minimally, we are asking that the temporary moratorium on the use of unfairness in rulemaking concerned with the content of commercial advertising be made a permanent part of the Federal Trade Commission Act. We have not prepared any specific language to accomplish that end for the proposal which we now offer would prevent application of the unfairness doctrine in both rulemaking and in case-by-case adjudication.

Here is our proposal. We propose that the Federal Trade Commission Act be permanently amended to provide that the term "unfair . . . acts or practices" does not apply to commercial speech.

We have two basic reasons for recognizing this constitutionally dictated protection for commercial advertising. The first reason is that it is needed to preclude the types of abuses which have taken place in the past. The second reason, obviously, is that advertising, unlike most other acts or practices within the FTC's jurisdiction, is a form of speech protected by the First Amendment to our Constitution. Let's take these two subjects up one at a time.

First, as to the need for the legislation. In 1979 this Committee's report on S. 1991 (S. Rep. No. 96-500, 96th Cong., 1st Sess.) explained the reason for denying the FTC funds to initiate any new rulemakings against advertising based on the unfairness doctrine by stating that the Commission has used its rulemaking power to: initiate [ ] proceeding in which the "unfairness" doctrine has been used as a broad charter for restricting commercial advertising solely because it may have consequences that the Commission finds objectionable or is otherwise contrary to the Commission's concept of "fairness". The breadth of this power—and its potential abuse—have been magnified considerably by the industrywide scope of the Commission's rulemaking authority. *Id.* at 17.

The Committee further explained that the legislation was intended: to redirect the Commission to its primary and long standing function of determining whether advertising contains representations that are false or have the capacity to deceive or mislead consumers. *Id.* at 18.

In passing, at this juncture, we should also point out that the Committee noted that the Commission's efforts to regulate truthful and non-deceptive commercial speech under the "unfairness" doctrine takes the Commission "into an area permeated by First Amendment concerns". *Id.* at 17.

While this Committee is well aware of the types of abuse heaped upon advertising by the Commission in the 1970's we would like to bring a few examples to your attention.

The most obvious example which immediately comes to mind is the Children's Television rulemaking effort which was brought to an end by congressional and Commission action. In the words of the then Chairman of the Commission, that rulemaking proceeding was premised on the concept that "children's advertising is inherently unfair". The remedies which the Commission would have imposed to correct this alleged unfairness would have, among other things, banned all television advertising of all products to very young children (probably under age 8) and would have banned the advertising of heavily sugared products to older children (probably under age 13). If that rule had gone into effect, it would have been unlawful to advertise baseball gloves, toys, cereal or any other product on, at least, Saturday morning television. Presumably you could not have advertised candy on any television program in which children made up a sizable percentage of the audience.

Several other trade regulation rule proceedings involved application of the unfairness doctrine to advertising. One of these proceedings, initiated November 11, 1975 (40 Fed. Reg. 52631), proposed a rule which would have made it unlawful to make an advertising claim for any over-the-counter drug which the Commissioner of Food and Drugs has determined may not be made in the labeling of the drug. If that rule had issued, it would have been "unlawful" to truthfully advertise a product, for example aspirin, as useful for backache, muscular aches and pains, menstrual pains or pain following tooth extraction if the FDA mandated label stated only that the product was good for headaches, occasional minor aches and pains and reduction of fever. Truthful advertising, completely devoid of deception, would have been suppressed.

Another example of overreaching is the Commission's completed and effective rule for Games of Chance in the Food Retailing and Gasoline Industries. Until last August, when it was changed, this rule prohibited a food store from conducting a second game of chance until it had waited a period equal to the length of time that its first game promotion ran. Thus if a food store had used a game promotion for six months it had to wait an additional six months until it could run a second such promotion. The Commission reasoned that the second promotion would be "unfair" because the consumers had become familiar with the first game promotion and would be confused by the second. This rule currently effectively bans the use of radio or television to advertise a game of chance promotion because it requires that the full details of the game's rules and all prizes and odds must be disclosed in all advertising—an obvious impossibility.

We could point out other examples of abuses such as the Food Advertising rulemaking procedure which was, in part, based upon unfairness. However to do so would merely burden the record for it seems unlikely that any reasonable person would dispute the fact that the Commission has, at least in rulemaking, used the unfairness doctrine in an abusive fashion.

At this juncture the logical question arises: If the abuses have been mainly confined to the rulemaking area, wouldn't it be adequate to merely make permanent the present temporary ban on the use of unfairness in rulemaking? Or, stated another way: Why does the advertising community feel that it is necessary to propose that Congress bar resort to the doctrine across the board, i.e., in both rulemaking and adjudications?

The short answer to these questions is that any act or practice the Commission can regulate in rulemaking it can regulate in case-by-case adjudications. If unfairness remains for advertising adjudications, a future Commission might decide to bring individual cases against advertisers based on the same unfairness theories which produced the aborted over-the-counter drugs and children's television rules. This would be a far worse situation for the advertisers subject to innovative orders to cease and desist would be at a competitive disadvantage with other sellers not subject to the orders. But, it can be argued, the Commission can take care of that by resorting to the procedure authorized in section 5(m)(1)(B) which permits it to go into district court and seek civil penalties agaisnt all of the other sellers who knowingly continue to advertise in a manner which violates the order issued against the first respondent. In our opinion that remedy is worse than the disease for, as we will point out later, it makes that first order to cease and desist tantamount to an industry-wide rule or statute without affording the industry any opportunity to comment or oppose.

The threat of a possible unfairness charge operates as an effective, chilling, prior restraint on inventiveness and innovation. Advertising is an art form. It must motivate and persuade or its cost constitutes an economic waste. Advertising must have freedom and elbow room to do its legitimate job and our proposal does no more than preserve the liberty which advertisers enjoyed until the Commission's recent "unfairness" initiative.

The Committee should also think of the economic costs which the FTC's pursuit of the unfairness doctrine imposes upon advertisers. It is not correct to say that no harm is done when the FTC goes off on one of these unfairness tangents but subsequently decides to abort the effort. Someone has to pay for that effort and in the final analysis it is the taxpayer, for the government's expense and the consumer, for the defendant's expenses.

Let us turn now to the constitutional, First Amendment question. As stated above, advertising is distinguishable from the other types of practices subject to the FTC's jurisdiction in that it, as a form of speech, enjoys a greater measure of constitutional protection. The proposition that truthful non-deceptive commercial speech was protected by the First Amendment was definitively announced by the Supreme Court in 1975 and 1976 in *Bigelow* v. *Virginia*, 421 U.S. 809 and *Virginia State Board of Pharmacy* v. *Virginia Citizen's Consumer Council, Inc.*, 425 U.S. 748. In *Virginia Pharmacy* the court concluded that the government may not "completely suppress the dissemination of concededly truthful information about entirely lawful activity . . . " 425 U.S. at 773. To state that the advertising community was elated by this long delayed First Amendment franchise understates the situation.

In the intervening years the Supreme Court in several holdings elaborated on the doctrine.[1] With these decisions firmly established as the law of the land the advertising community takes comfort in the fact that the First Amendment applies to advertising. Even though, in 1980, the Supreme Court, in *Central Hudson Gas & Electric Corp.* v. *Public Service Commission of New York*, 447 U.S. 557, made clear that constitutional protection of advertising is not absolute, in doing so it announced a four part test to be used in defining the limits of the constitutional protection of commercial speech.

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[1] *Linmark Associates, Inc.* v. *Willingboro*, 431 U.S. 85 (1977); *Bates* v. *State Bar of Arizona*, 433 U.S. 350 (1977); *Friedman* v. *Rogers*, 440 U.S. 1 (1979).

The first test is to initially determine whether the advertising is true or false. If it is false that ends the matter for false advertising is not protected by the First Amendment. In our opinion, if the advertising is true, i.e., non-deceptive, that should also end the matter but, unfortunately, that is not what the court held. It went on to declare the remaining three parts of the test which any government ban on truthful advertising must pass if it is to withstand constitutional scrutiny. In essence the tests are (1) whether a substantial government interest is served by the regulation, (2) whether the regulation "directly advances" the asserted public interest and (3) whether the proscription is overly broad or would some lesser remedy be sufficient.

Predictably, it did not take the Commission long to seize upon *Central Hudson* as a license for it to preempt the congressional and presidential prerogative of articulating substantive governmental interest in interstate commerce and determining what restrictions are necessary to directly promote them without being more restrictive than needed. In its letter to this Committee of December 17, 1980, the Commission announced: "To the extent that it may need to exercise such [unfairness] authority in the future, it will do so in conformity with the standards established in *Central Hudson.*"

In its letter of November 13, 1979 to Senator Ford the FTC Commissioners charge that excision of their alleged authority to regulate speech on grounds of "unfairness" would adversely affect their ability to protect children from physical dangers created by advertising. In support of this argument they refer to several consent orders to cease and desist which are ostensibly based upon the "unfairness" theory. These consent orders interdicted advertisements which depicted youthful models carelessly riding bicycles on busy streets;[2] depicted a naturalist eating unidentified wild berries or fruits,[3] and depicted a child cooking rice on a gas stove.[4] Whether these proceedings were based upon the theory of "unfairness" is somewhat questionable for each of the complaints charged that the advertising practice was an unfair and deceptive act or practice. These cases were not litigated and therefore do not demonstrate that the Commission would have been powerless to challenge the advertisements even if the word "unfair" were not in its statute. Indeed, classic principles of deceptiveness should be adequate to cover any advertisement that falsely misleads children.

THE COMMISSION SHOULD NOT HAVE THE POWER TO EMPLOY BACK DOOR RULEMAKING

We will now return to a subject we briefly mentioned earlier in our statement. We believe and strongly urge that section 5(m)(1)(b) of the Federal Trade Commission Act should be repealed. We believe that this provision, which authorizes the Commission to bring enforcement proceedings in district courts against advertisers who violate orders to cease and desist produced by adjudicative proceedings in which they were not parties, constitutes "back door rulemaking". As we see it the Commission could decide to forego rulemaking under section 18 of the Act since it has this handy loophole to force its will upon an entire industry.

The rulemaking safeguards of the Magnuson-Moss Act were imposed to ensure that the affected industry had an opportunity to defend itself. As the drafters of the procedural safeguards put it: Because of the potentially pervasive and deep effects of rules defining what constitutes unfair or deceptive acts or practices and the broad standards which are set by the words "unfair or deceptive acts or practices", the Committee believes greater procedural safeguards [than mere notice and comment] are necessary.[5]

If the actual giving of notice and the opportunity to file comments in a rulemaking proceeding were deemed inadequate, it seems obvious that the complete absence of these opportunities as sanctioned by section 5(m)(1)(B) is intolerable. In its report on S. 1991[6] this Committee noted that it "is aware that a potential ambiguity may be presented to the Commission with respect to its enforcement authority under section 5(m)." The Committee promised a thorough review of this ambiguity when it next considered the issue of "unfairness". We urge that review can and should have only one result, the repeal of section 5(m)(1)(B).

This section hangs like a "sword of Damocles" over the heads of all advertisers. The Commission's chilling use of it, and apparent intent to wield it is evident in its widespread *in terrorem* circulation of extant cease and desist orders to the industries involved, with its unmistakable implications. We are concerned that the section affords the Commission leeway to select some small or complacent company as a target, exact from it a consent or weakly litigated order to cease and desist and then enforce the order against an entire industry. This is not the way industry-wide rules should be promulgated for it makes a mockery of the due process rights of advertisers and other businessmen.

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[2] A.M.F., Inc., File No. 782-3025, 1979 Trade Regulation Reports ¶51,589.

[3] General Foods Corp., 86 F.T.C. 831 (1975).

[4] Uncle Ben's, Inc., 89 F.T.C. 131 (1977).

[5] H. Rep. No. 93-1107, 93rd Cong., 2d Sess., May 17, 1973, p. 45.

[6] S. Rep. No. 96-500, 96th Cong., 1st Sess., Dec. 14, 1979, p. 18.

We greatly appreciate this opportunity for the advertising community to present its views on these important subjects.

[The following information was subsequently received for the record:]

Advertising Is Speech Protected by the First Amendment, So the Federal Trade Commission's Authority To Regulate or Proscribe "Deceptive" Advertising Must Be Clarified

Our democracy and our marketplace are grounded upon the conviction that wise decisions are most likely to be made when a broad range of information is desseminated. The First Amendment thus stands to protect the free flow of information. Communication does not take place without a receiver as well as a sender, so the right of all to speak freely implies an equal right on the part of the public to hear those who would speak. Indeed, the freedom to learn, to be fully informed on matters of interest, is a precious an inheritance as the freedom to tell.

Therefore, the guarantees of the First Amendment reach beyond the individual speaker to encompass, as well, the recipient of the communication. As the Supreme Court summarized in a case which invalidated as unconstitutional a Virginia statute prohibiting the advertising of prices of prescription drugs, "[i]f there is a right to advertise, there is a reciprocal right to receive the advertising." *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 757 (1976). See *Red Lion Broadcasting Company* v. *FCC*, 395 U.S. 367, 390 (1969); *Stanley* v. *Georgia*, 394 U.S. 557, 564 (1969); *Martin* v. *Struthers*, 319 U.S. 141, 149 (1943). While the persuasive aspect of commercial advertising may be of particular value to sellers of goods or services, the informational content is no less significant to consumers, whose knowledge of product availability would be restricted in the absence of advertising. The public's understanding varies with the quantity and quality of its information. As a consequence, the Supreme Court's decisions involving corporations which have undertaken to communicate with a segment of the public are appropriately based: "not only on the role of the First Amendment in fostering individual self-expression but also on its role in affording the public access to discussion, debate, and the dissemination of information and ideas.

First National Bank of Boston v. *Bellotti*, 435 U.S. 765, 783 (1978) (footnote omitted) (citing cases).

We submit that under Constitutional principles, commercial speech—advertising—cannot be restricted or proscribed unless: a court determines that it is deceptive, or the restriction directly serves a substantial governmental interest and the restriction does not exceed what is necessary to serve that interest. As the Supreme Court has explained in the context of advertising for professional services,

"Commercial speech doctrine . . . may be summarized generally as follows: Truthful advertising related to lawful activities is entitled to the protections of the First Amendment. But when the particular content or method of the advertising suggests that it is inherently misleading or when experience has proven that in fact such advertising is subject to abuse, the states may impose appropriate restrictions. Misleading advertising may be prohibited entirely. * * * Even when a communication is not misleading, the state retains some authority to regulate. But the state must assert a substantial interest and the interference with speech must be in proportion to the interest served. *Central Hudson Gas Co.* v. *Public Service Comm'n*, 447 U.S., at 563–564. Restrictions must be narrowly drawn, and the state lawfully may regulate only to the extent regulation furthers the state's substantial interest. *In the Matter of R.M.J.*, 102 S. Ct. 929, at 937–38 (1982) (footnote omitted)."

Consequently, we respect and endorse the suggestions of Chairman Miller and a number of concerned organizations that the FTC Act include an explicit definition of what constitutes a "deceptive act or practice." The need for such a definition has also been pointed out by Professor Rosden in his treatise The Law of Advertising:

"It has been said sometimes, and not without a measure of truth, that an advertisement is deceptive if the Federal Trade Commission calls it so. This situation, unusual as it is in American jurisprudence, is due to a combination of reasons. In the first place, Congress has not seen fit to set legislative standards that have an ascertainable degree of definiteness.

"Nor has Congress written standards into the Act after several decades of administrative and judicial ad hoc interpretations. Section 18.03, pp. 18-46 to 18-47."

Timothy Muris, the Director of the Commission's Bureau of Consumer Protection, has also endorsed the need for clarification of the Commission's overbroad and unconstrained authority to censor advertisements as deceptive. In his memorandum filed with this Subcommittee with Chairman Miller's Separate Statement of April 1, 1982, he concluded:

"Because the current Section 5 legal standard is so broad and ambiguous, case selection has been a time-consuming and recurrent problem. Because the Commission *can* do almost anything, the question has always been what *should* it do? Ideally, a body of law should clearly characterize a central core of transactions that will always result in liability.

* * * * * * *

"Throughout its controversial 68 year history, the FTC has never quite fulfilled its promise of providing consistent and substantial protection to consumers. The fault lies not in the fine people who have served here, but instead in the overly broad standards that Congress has provided us—standards that do not provide guidance on how to proceed. With these broad standards, in one era the Commission did little, focusing largely on trivia. In the next, the Commission took upon itself the mantle of the second most powerful legislature in America, surely a task inappropriate for five unelected officials. Muris Memorandum, at 26-27, 29."

The examples contained in the Muris Memorandum of Commission overreaching in this area, and a host of others that could be added, clearly support the need for congressional action. To do so, we recommend that the Act include a provision clarifying that:

"Deceptive acts or practices in or affecting commerce are declared unlawful where such acts or practices—

"(1) consist of material representations known to be false or made in reckless disregard of their truth or falsity, or

"(2) consist of misrepresentations that directly cause or may forseeably result in substantial economic injury to consumers acting reasonably in the circumstances."

We emphasize that any definition should require advertisers to act responsibly and should reinforce the requirement for bona fide ad substantiation. While we believe that such a definition would help to clarify the Act, we submit that the amended Act would still fall far short of what the Constitution requires if it leaves the Commission free to apply the amorphous "unfairness" doctrine to commercial speech.

WEITZMAN & ROGAL, 1320 NINETEENTH STREET, N.W.,
Washington, D.C., March 22, 1982.

Hon. BOB KASTEN,
Chairman, Subcommittee on Consumer, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

DEAR CHAIRMAN KASTEN: Near the close of my testimony on Friday you asked me to enlarge upon my contention that elimination of the "unfairness doctrine" as applied to commercial speech would not impair the Commission's powers to insist that affirmative advertising claims must be substantiated by factual support such as would satisfy a reasonably prudent advertiser as to the truth. I stated that one who makes a specific, affirmative claim as to a product's attributes clearly represents or implies to the consumer that he has conducted tests or surveys or has some other basis for making the claims. That representation or implication is false, i.e., deceptive if he in fact lacks such material. The Commission's own decisions and the only court cases reviewing advertising substantiation orders to cease and desist support this view.

The story begins in 1963 when the Commission issued an order against Heinz W. Kirchner[1] who had represented that his inflatable swimnming device rendered the user "unsinkable". The respondent had no evidence to back up this claim and the Commission held:

"One who affirmatively advertises a product to be safe, in a context in which the prospective user's health or safety may be adversely affected if the claim is false, implicitly represents that he has a reasonable and substantial foundation in fact for making the claim.

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[1] 63 F.T.C. 1282, aff'd. 337 F.2d 751 (9th Cir., 1964).

The first court case which involved review of an advertising substantiation order is the same case which was discussed at such great length at the hearing on Friday, *Firestone Tire & Rubber Co.* v. *FTC*, 481 F.2d 246 (6th Cir., 1973). As you know one of the advertising claims challenged by the Commission was that the respondent's wide oval tires will cause a car to "stop 25 percent quicker." The Commission found that this claim implied that the respondent had conducted scientific tests. Firestone disputed this finding but the court held:

"As to the first of these issues, we believe the Commission did find that the "Stops 25 Percent Quicker" ad implied scientific testing. It said: In the circumstances of *this* case, we believe that consumers could reasonably have expected Firestone's performance and safety claims to have been substantiated by scientific tests.

"In addition, we think such an implication is entirely reasonable from the comparison and percentage language employed."

The court went on to find that the stopping claim was "unfair and deceptive to consumers" because it was "without substantial scientific test data to support it."

Perhaps the most convincing illustration of my premise that advertising substantiation cases are not dependent upon the unfairness doctrine is *Porter & Dietsch Inc., et al.*, decided by the Commission on December 20, 1977. C.C.H. transfer binder at ¶ 21,380. The case involved a weight reduction product and advertising substantiation was one of the principal issues in controversy. As the Commission said: "The primary question thereby put in issue by the complaint is not whether the claims of weight loss are false but instead whether, at the time they were made, respondents possessed reasonable substantiation for them."

After reviewing this question at great length the Commission concluded:

"We conclude that respondent's advertising is *false and misleading*, because it implicitly represents that "substantially all users of X-11 tablets will lose a significant amount of weight" and that respondents possess competent scientific evidence supporting that claim, even though respondents did not have a reasonable basis for making such a claim at the time the advertising was disseminated." (Emphasis supplied.)

Please note Senator that the Commission did not even use the word "unfair". The advertisements were found to be "false and misleading" because they implied, contrary to fact, that the respondents possessed competent scientific evidence to support the claims at the time they were made. The Commission's decision was affirmed by the 7th Circuit Court of Appeals on August 8, 1979. 1979-2 Trade Cases ¶ 62,796.

My colleagues and I appreciated the opportunity to present the advertising community's views to the Committee. If we can be of further assistance to the Committee or its staff please let us know.

Sincerely,

WILLIAM W. ROGAL.

Senator **KASTEN**. Mr. David Greenberg, legislative director, Consumer Federation of America.

Mr. **GREENBERG**. Thank you, Mr. Chairman, Senators.

The Consumer Federation of America appreciates this opportunity to present its views concerning the FTC's unfairness authority as it affects advertising practices. I would like to add that the AFL-CIO has asked me to tell you that they join in these remarks.

In the Federal Trade Commission Improvements Act of 1980, the Congress adopted language prohibiting the Commission from promulgating rules affecting advertising that derived from the unfairness authority. We have just heard that the advertising industry will seek to extend the life of that special exemption and broaden its reach to encompass adjudications.

We are strongly opposed to this effort, and urge Congress to reject this attempt by advertisers to carve out a separate and distinct category for themselves that they alone will occupy. We believe the unfairness authority has served a useful function, both in protecting the interests of consumers and in promoting the more effective functioning of the market.

Historically, Mr. Chairman, Congress has determined that administrative agencies must possess sufficiently broad legal authority if they are to effectively carry out their responsibilities. This authority has enabled bodies such as the FTC, which retains responsibility for economic regulation, to respond quickly and creatively to the ever-changing commercial practices that are characteristic of a dynamic marketplace.

In the case of the FTC, the need for flexibility in the formulation and application of the Commission's unfairness authority was recognized by the framers of the FTC Act themselves. They wrote nearly 70 years ago that, and I quote:

> It is impossible to frame definitions which embrace all unfair practices. There is no limit to human inventiveness in this field. Even if all known unfair practices were specifically defined and prohibited, it would be at once necessary to begin over again. If Congress were to adopt the method of definition it would undertake an endless task.

By prohibiting the FTC from employing its unfairness authority, which it has used well in the past, the Congress will inevitably limit the Commission's ability to deal effectively and constructively with an industry, advertising, that has been characterized by constant change. One of the most frequent phrases of our time involves the communications revolution, of which advertising is obviously a significant part. Consider the list of innovations in advertising practices and in communications technology that our society is presently and will continue to experience.

Examples include the long form commercial or the infomercial that is emerging as a means of capitalizing on cable TV's particular capabilities. There is also the video catalog concept being test marketed by Warner Cable and American Express that represents the telecommunications industry's efforts to meet the rising demand for direct marketing. There is also the telephone computer service, known as The Source, that home viewers may soon be able to use to make purchases from home.

These technological changes and others like them will provide consumers with a mind-boggling array of new benefits and opportunities, but it will also expose them to some new risks that we are incapable of anticipating. It is just this kind of technological advance that requires the Congress, we believe, to continue to vest broad authority in regulatory agencies, authorities such as unfairness, if we are to cope with dramatic changes while suffering the least amount of harm.

The unfairness authority has already proven useful in allowing consumers to exercise a more informed judgment about a relatively unfamiliar product whose quality depended primarily on a single factor. In promulgating its trade regulation affecting the marketing of insulation, the Commission required advertisers to disclose the product's R value, which is a measure of heat retention, if price or insulating ability was mentioned in the advertisement. To issue this rule, the Commission relied heavily, although not exclusively, on its unfairness authority.

Can we really conclude with any sense of certainty that there will be no products created in the future where the need to provide the consumer with essential information will best be met by the use of the Commission's unfairness authority? In addition, as well as its ability to draw on its unfairness authority in the field of advertising, the Commission has been able to more effectively protect the safety of our most vulnerable citizens. The Commission has negotiated a series of consent decrees that have reduced the likelihood that young children will expose themselves to harm as the result of advertising-induced imitation behavior.

In Meco International, for example, the Commission barred an advertisement showing the children playing with electrical appliances near water. Critics will contend that the FTC's authority to take action against deceptive advertisement is sufficient to cover the cases referred to. We disagree.

First, one cannot be certain that absent the unfairness authority the existing deception power will prove capable of dealing with advertisements, encouraging vulnerable groups, such as children, to engage in unsafe or illegal behavior.

To quote Commissioner David Clinton:

> It would stretch the meaning of the section beyond all normal usage to say that every instance of coercion, every failure to live up to a bargain, and every use of overreaching is inherently deceptive. Practices that are reasonable in most situations may have a potential for unfairness in certain limited circumstances. That may be true, for example, where the target audience is especially susceptible or vulnerable to the appeal of particular products or services. Such an audience might consist of children, the elderly, the lonely, or the unemployed.

In weakening the Commission's authority to act, the Congress may well be allowing some of society's most vulnerable citizens to fall through the newly created cracks. Additionally, we believe that there are some commercial practices that warrant discouragement by our society despite their score on a narrow cost-benefit basis. On this point, we find the comments of Stanley Cohn, the Washington editor of Advertising Age, and an individual who brings decades of experience to these issues, particularly instructive. In the March 8 1982, issue of that publication, Cohn wrote:

> The FTC's duty is not to the defrauded consumer alone, but to the marketplace itself. The Commission is less concerned about the size of the injury than it is about the morality of the practices that prevail. Only nominal consumer injury was caused by advertising for Palmolive Shave Creme, Pfizer Unburn, and Listerine, yet the ban on TV demonstrations, the ad substantiation doctrine, and the concept of corrective advertising established by these cases moved advertising ethics from the flim-flam that prevailed in the 1960's to the laudable standards that exist today.

The quote continues:

> Palmolive Rapid Shave, Unburn, and Listerine led to a new ethic which encourages consumers to respect advertising people and to trust advertising. Advertisers get a bigger bang for their advertising buck. Prices are lower because effective advertising holds selling costs down. How do these valuable considerations survive once the law is amended so that the FTC deals only with advertising cases where the injury to consumers exceeds the countervailing benefits?

In summary, Mr. Chairman, we believe that Congress should not reduce the ability of the Federal Trade Commission to deal with unfair or deceptive advertising practices. In general, consumers as well as legitimate advertisers and honest businessmen have been well served by the Federal Trade Commission's exercise of its authority in this area. It would be tragic if in its attempt to restrain the activities of the Federal Trade Commission the Congress punished the public instead.

Thank you.

[The statement follows:]

STATEMENT OF DAVID I. GREENBERG, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA

Mr. Chairman, Members of the Subcommittee, the Consumer Federation of America appreciates this opportunity to present its views concerning the Federal Trade Commission's "Unfairness" authority as it affects advertising practices. In addition to our comments on this matter, we have prepared written remarks regarding other issues that are likely to be considered during the course of the debate over the Commission's authorization. With your permission, we would like to submit these comments for the record.

In the Federal Trade Commission Improvements Act of 1980, the Congress adopted language prohibiting the Commission from promulgating rules affecting advertising that derived from the "Unfairness" authority. It is our understanding that the advertising industry will seek to extend the life of that prohibition, and broaden its reach to encompass adjudications. The Consumer Federation of America is strongly opposed to this effort, and urges the Congress to reject this attempt by advertisers to carve out a separate and distinct category for themselves that they alone will occupy. We believe the "Unfairness" authority has served a useful function both in protecting the interests of consumers and in promoting the more effective functioning of the market.

Historically, Mr. Chairman, the Congress has determined that administrative agencies must possess sufficiently broad legal authority if they are to effectively carry out their responsibilities. This authority has enabled bodies such as the Federal Trade Commission, which retain responsibility for economic regulation, to respond quickly and creatively to the everchanging commercial practices that are characteristic of a dynamic marketplace. In the case of the FTC the need for flexibility in the formulation and application of the Commission's "Unfairness" authority was recognized by the framers of the FTC Act themselves. They wrote, nearly seventy years ago, that: "It is impossible to frame definitions which embrace all unfair practices. There is no limit to human inventiveness in this field. Even if all known unfair practices were specifically defined and prohibited, it would be at once necessary to begin over again. If Congress were to adopt the method of definition, it would undertake an endless task."

By prohibiting the Federal Trade Commission from employing its "Unfairness" authority, which it has used well in the past, the Congress will inevitably limit the Commission's ability to deal effectively and constructively with an industry, advertising, that has been characterized by constant change. One of the most frequent phrases of our time involves the "communications revolution", of which advertising is obviously a significant part. Consider the list of innovations in advertising practices and in communications technology that our society is presently, and will continue to experience. Commissioner Pertschuk touched on this subject in a speech he delivered on the "Media Explosion" some two years ago, where he briefly described some of the new services and products that were on the verge of being offered to consumers. "There is the long-form commercial, the infomercial, that is emerging as a means of capitalizing on cable's particular capabilities. There is the video catalogue concept being test-marketed by Warner Cable Company and American Express that represents the telecommunications industry's efforts to meet the rising demand for direct marketing. There also is the telephone computer service, known as 'The Source', that home viewers soom may be able to use to make purchases from home. There is the advanced viewdata system, such as the British Post Office's Prestel, which can provide on the spot access to comparative price and performance data for a product." These technological changes will provide consumers with a mind-boggling array of new benefits and new opportunities, but it will also expose them to risks that we are incapable of anticipating. It is just this kind of technological advance that requires the Congress, we believe, to continue to vest broad authority in regulatory agencies, authority such as "Unfairness", if we are to cope with dramatic changes while suffering the least amount of harm.

The "Unfairness" authority has already proven useful in allowing consumers to exercise a more informed judgment about a relatively unfamiliar product whose quality depended primarily on a single factor. In promulgating its trade regulation affecting the marketing of insulation, the Commission required advertisers to disclose the product's R-Value (a measure of heat-retention capability) if price or insulating ability was mentioned in the advertisements. To issue this rule, the Commission relied heavily, although not exclusively on its "Unfairness" authority. Can we really conclude, with any sense of certainty, that there will be no products created in the future where the need to provide the consumer with essential information will best be met by the use of the Commission's "Unfairness" authority?

As result of its ability to draw on its "Unfairness" authority in the field of advertising, the Commission has been able to more effectively protect the safety of our most vulnerable citizens. The Commission has negotiated a series of consent decrees that have reduced the likelihood that young children will expose themselves to harm as the result of advertising-induced imitative behavior. In *Mego International*, for example, the Commission barred an advertisement showing children playing with electrical appliances near water without adult supervision. Similar cases include *Uncle Bens, Inc., AMF, Inc.*, and *General Foods Corporation.*

Critics of "Unfairness" will contend that the FTC's authority to take action against "deceptive" advertisments is sufficient to cover the cases referred to in the preceding paragraph. We disagree.

First, one can not be certain that absent the "Unfairness" authority, the existing deception power will prove capable of dealing with advertisements encouraging vulnerable groups, such as children, to engage in unsafe or illegal behavior. To quote Commissioner David Clanton, in a speech before the San Diego Advertising Club, in March, 1980, "It would stretch the meaning of deception beyond all normal usage to say that every instance of coercion, every failure to live up to a bargain, every use of overreaching is inherently deceptive. . . . Practices that are reasonable in most situations may have a potential for unfairness in certain, limited circumstances. That may be true, for example, where the target audience is especially susceptible or vulnerable to the appeal of particular products or services. Such an audience might consist of children, the elderly, the lonely or the unemployed." In weakening the Commission's authority to act, the Congress may well be allowing some of society's most vulnerable citizens to fall through the newly created cracks.

Moreover, there is no assurance that the FTC will emerge from this authorization battle with its "Deception" authority fully intact. After all, even if the advertisers do not seek to weaken the "Deception" power, this does not prevent other elements of the business community, or the present Chairman, from acting to narrow its scope. The elimination of the "Unfairness" authority, coupled with a weakening of the Commission's ability to deal with deception, could well leave many kinds of advertisements, including those mentioned above, immune from legal action by the FTC. In effect, a twin blow to the unfairness and deception authority would give advertisers a virtual exemption from the act.

On a number of occasions, the industry has argued that self-regulation has reduced the need for legal intervention. But self-regulation, Mr. Chairman, does not occur in a vaccum. It is often the initiative of an effective Federal agency that causes industry to act. Several years ago, for example, the agency appeared on the verge of moving against television advertising of vitamins to children. Before final action could be taken, however, the potential respondents voluntarily ceased advertising vitamins to home audiences that were likely to be comprised largely of children. Soon after this, the National Association of Broadcasters Code was amended to prohibit televised vitamin advertising to children. Moreover, we believe that the continued presence of reasonably effective self-regulation, rests as the trade journal *Advertising Age* stated, "on the existence of a vigorous FTC . . . when FTC retreats, it exposes the self-regulation flank."

In the days before these hearings, Mr. Chairman, there has been some indication that the business community might choose an alternative course of action in its attempts to constrict the agency's authority. Instead of seeking complete exemption from the "Unfairness" power, industry might attempt to require the Federal Trade Commission to conduct a formal cost/benefit analysis before it could take action against either an unfair or deceptive practice, or to prove culpable knowledge and economic injury before preventing a deceptive practice, as Chairman Miller has proposed. For a number of reasons, which we will expand upon in our written statement, we believe the imposition of such requirements would do considerable more harm than good. To meet these new preconditions before taking action, the Commission would have to divert more of its already declining resources away from its primary responsibilities, the protection of consumers and the promotion of competition.

Additionally, we believe that there are some commercial practices that warrant discouragement by our society, despite their possible economic utility. On this point, we find the comments of Stanley Cohen, the Washington Editor of Advertising Age, and an individual who brings decades of experience to these issues, particularly instructive. In the March 8, 1982 issue of that publication, Cohen wrote: "FTC's duty is not to the defrauded consumer alone but to the marketplace itself. The Commission is less concerned about the size of the injury than it is about the morality of the practices that prevail . . . Only nominal consumer injury was caused by advertising for Palmolive shave cream, Pfizer's Unburn and Listerine. Yet the ban on phony TV demonstrations, the ad substantiation doctrine and the concept of corrective advertising established by these cases moved advertising ethics from the flim flam that prevailed in the 1960's to the laudable standards that exist today . . Palmolive Rapid Shave, Unburn and Listerine led to a new ethic which encourages consumers to respect advertising people and to trust in advertising. Advertisers get a bigger bang for their advertising buck. Prices are lower because effective advertising holds selling costs down. How do these valuable considerations survive once the law is amended so FTC deals only with advertising cases where the injury to consumers exceeds the countervailing benefits?"

In summary, Mr. Chairman, we believe the Congress should not reduce the ability of the Federal Trade Commission to deal with unfair or deceptive advertising practices. In general, consumers as well as legitimate advertisers and honest businessmen have been well served by the Federal Trade Commission's exercise of its authority in this area. It would be tragic, if in its attempt to retrain the activities of the Federal Trade Commission, the Congress punished the public instead.

Thank you.

In our oral statement, we addressed question relating to the Federal Trade Commission's legal authority and its effect on advertising. At this time, we would like to deal with a couple of other controversial issues that will no doubt be a subject of intense controversy as the debate over the FTC's authorization continues.

PROFESSIONALS

In the debate over the extension of the FTC's authorization in 1980, considerable attention was focused on the Commission's jurisdiction over the professions. It appears that the vehicle for the continuation of that debate exists in the form of S. 1984, the McClure-Melcher bill, which contains language which would totally exempt from Commission study, rulemaking and prosecution all activity of "practioners of a profession whose members are licensed and regulated by a state as a condition of independent practice within the state . . ."

The Consumer Federation is strongly opposed to this portion of the McClure-Melcher bill, which would more appropriately be titled the "Profession's Income Maximization Act of 1982."

The range of professions likely to be covered by this legislation is virtually without limit, running the gamut from doctors and lawyers to accountants and engineers. To eliminate the Federal Trade Commission's ability to deal effectively with the activities of these professions, will, in effect, cause consumers to continue to be the victims of a variety of practices that have curtailed competition and impeded the flow of information without improving the quality of the services provided. The costs associated with these practices are significant. Health care expenditures alone accounted for nearly 10 percent of the Gross National Product in 1980.

We are gratified that Chairman Miller has urged the Congress to reject this attempt to, as he has written, grant "state-regulated professionals (and associations of professionals) immunity from law enforcement that others do not enjoy." It indicates that he is distinctly aware of the need for a continuing active Commission presence in this area. Just last year, a new report on this issue, titled "Self-Regulation In the Professions, was prepared for the National Science Foundation. In describing its contents, Regulation" magazine noted that the report concluded that the professions "remain in control of the organization of their work." Regulation goes on to comment: "Where there have been changes, they have often been in the direction of tighter controls on entry and added requirements for those in the field—the opposite of what many reformers have called for." Again, the Consumer Federation of America urges the Congress to oppose a special exemption for the professions.

COST-BENEFIT ANALYSIS

As we mentioned in our oral statement, it is quite possible that, as the debate over the FTC's authorization progresses, there might be a concerted effort by the business community to formally require the Commission to conduct a cost/benefit analysis before it proceeds against an "unfair" or "deceptive" practice. One such proposal would force the Commission to demonstrate that the costs of a practice must not be "outweighed by countervailing benefits to consumers or competition" before such practice can be declared unlawful.

We oppose adding this kind of analytical burden to the procedures that the Commission already follows. There is a considerable, and critical difference between ensuring that the Commission includes an assessment of potential costs and benefits as one factor in a number of considerations and requiring the agency to take no further action unless the results of a cost/benefit analysis are favorable. As Peter A. Schuck, no reflexive supporter of regulation, has written: "Anybody who suggests that it should be plugged in mechanically to generate a result that a decision-maker must accept is either misinformed or a fool . . . I know of no regulators who are not well aware of the imperfections of cost-benefit analysis; nor do I know any regulators who view cost-benefit analysis as anything more than a sometimes useful, but almost never decisive, tool."

Unfortunately, in some quarters, cost-benefit analysis' "imperfections" are not given sufficient consideration and attention; instead, it is advertised as an objective tool for determining the correctness of an agency's action. We believe the "neutrality" of cost-benefit analysis remains to be demonstrated.

Consider, for example, the remarks of George Eads, an economist whose involvement in regulatory matters began during the Ford Administration. Last year, at a hearing conducted by the House Commerce Oversight and Investigations Subcommittee, Eads commented on the fate that met a number of regulatory actions shortly after the Reagan Administration came to power. Eads stated: "For example, the OSHA noise regulation, which, in my opinion, was very well supported by the agency, not only on feasibility grounds but on grounds of cost-effectiveness and cost-benefit, was held up just the same as any others. The Food and Drug Administration's patient package insert regulations were also held up despite good economic support. . . .

"However, the White House is already claiming cost savings from diesel particulate regulations, emissions average, and a number of things, where, when we in the Carter Administration looked at them, a record was nonexistent . . . The White House seems to have already decided what the conclusion in the rulemaking should be.

"If the agencies are not adequately supplied with analytical resources or if, whether intentionally or inadvertently, they are signaled that the analyses they do produce do not matter, the cause of regulatory reform will be set back seriously."

Other shortcomings exist, that, we believe, compel caution by the Congress before it chooses to make the cost/benefit test "first among equals" in determining regulatory policy. Because cost/benefit analysis fails to take into consideration technological change or economies of scale, the cost of a regulation tends to be overstated. Moreover, costs cannot be measured solely in the aggregate; instead they are allocated between classes, the rich and the poor, and the old and the young. Thus, in some cases, value judgments must inevitably come into play when a regulator is attempting to predict the impact of a policy decision. Additionally, many benefits produced by a regulation are extremely difficult, if not impossible to quantify. To paraphrase Standly Cohen, the Washington Editor of Advertising Age: how can we measure the benefits the business community receives because public faith in the marketplace has risen as a result of reasonable regulatory initiatives encouraging honest dealings?

Considering the kind of limitations inherent in cost/benefit analysis, we believe the Congress should refrain from imposing this kind of crippling procedural requirement on the Federal Trade Commission.

Senator **Kasten**. Next is Mr. Ernest Pepples. Mr. Pepples, we apologize for misspelling your name.

Mr. **Pepples**. Thank you very much.

I am here for Brown & Williamson, and also Saks Fifth Avenue, Gimbels, and Kohl Supermarkets, all of whom are major advertisers in their markets. We are offering a statement which I believe has been picked up in a recent bill. At least the bill that Senator Cannon has introduced, I am informed, is very close to our proposal to extend the prohibition on unfairness as a basis for controlling nondeceptive ads into section 5 as well as maintaining the prohibition with respect to rulemaking. It is S. 2221.

In 1980, the legislation that Congress enacted placed a temporary prohibition on the use of unfairness against advertising. We believe that prohibition should be made permanent and should be incorporated in section 5 so that it applies both to adjudicative as well as to rulemaking processes. So, the sole purpose, in effect, of this proposal is to eliminate the basis for the censorship that the Commission exercised in what we believe was a recent and really unprecedented assertion of authority.

I believe that problems of similar magnitude and importance do not exist with respect to the Commission's jurisdiction to prevent other unfair methods of competition and unfair acts or practices, and my statement does not address the issue of changing the unfairness standard in the context of nonadvertising practices, but is limited exclusively to protecting free commercial speech.

The second part of my statement deals with rulemaking, and I would just say very briefly that I think rulemaking is where the FTC had its greatest trouble both before this body and before the courts. It has historically been an enforcement agency and not a regulatory agency in the accepted sense. I think the best thing that Congress could do would be to return it to its traditional role.

I think there is a place for an umpire, the man in the striped shirt. This is a good horse, and when I testified in 1979, I indicated that our feeling was, the horse had a burr under the saddle. It had thrown the rider, and it was off the track, that it was nevertheless an important animal, one that was necessary to prevent unscrupulous businessmen from taking advantage of their competitors and certainly taking advantage of consumers.

I think that the hearings that were held by this committee and the steps that were taken by the Congress have made great progress. We have not heard all morning any reference to the "national nanny." I think that there has been a change in attitude at the Commission, and I think it is due in great degree to the things that the Congress has done and the things that have transpired in the last few years, but I think it would be a mistake to allow the 1980 prohibition against overregulation of advertising to expire.

So, the statement that I have offered on behalf of these companies urges you to make the unfairness jurisdiction apply only to non-advertising practices.

And we would urge that the rulemaking power under Magnuson-Moss be eliminated. If that is not possible, then we have pointed to one of the phrases in that statute, Magnuson-Moss, tucked way down at the bottom of the pertinent subsection, which allows the Commission to prescribe affirmative requirements for entire industries. In effect what happens under a rule that contains requirements for a whole industry is something very close to the NRA-type of rulemaking. In other words, it becomes a straightjacket tailored for the one bad actor but fastened onto everyone. I think that while eliminating that one sentence, and I will quote the sentence, that you would in effect be—you would be pulling back some of the overly broad legislative powers that were granted to FTC.

I refer to the ancillary authority contained in the act to include in rulemaking, which defines unfair or deceptive acts or practices, additional affirmative requirements "prescribed for the purposes of preventing such acts or practices." That provision should be eliminated.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF ERNEST PEPPLES

My name is Ernest Pepples. I am Senior Vice President and General Counsel of Brown & Williamson Tobacco Corporation of Louisville, Kentucky. Brown & Williamson is a wholly-owned subsidiary of BATUS Inc., a holding and management corporation with substantial interests in the tobacco, retailing and paper industries. Other BATUS subsidiaries include Gimbels Department Stores, Saks Fifth Avenue, Kohl's Food Stores and Kohl's Department Stores, and Appleton Papers, Inc. I am submitting this statement on behalf of the entire BATUS group.

Most of the operations of this group of companies are in highly competitive consumer-serving industries in which advertising plays an important role, and we are pleased, therefore, to have this opportunity to present our views to you on legislative subjects which have a profound influence on our business.

I appeared before this Subcommittee in September 1979 during hearings on an earlier FTC authorization bill which resulted in the FTC Improvements Act of 1980. The statement I submitted then remains pertinent to these current hearings. Therefore, I shall endeavor to keep this statement brief, and shall address only two subjects.

The first subject is unfairness and advertising. In the 1980 legislation Congress enacted a temporary prohibition on Commission regulation of advertising on the basis of unfairness, but limited the prohibition to rulemaking. The prohibition should be made permanent and should be incorporated in section 5 so as to eliminate "unfairness" as a basis for regulating advertising content in any proceeding, whether adjudication or rulemaking. I do not perceive problems of the same magnitude and importance with respect to the Commission's jurisdiction to prevent other unfair methods of competition and unfair acts or practices, and I have not addressed the issue of changing the unfairness standard in the context of non-advertising practices.

The second subject I want to address is rulemaking. Legislative rulemaking by the FTC, expressly authorized by the Magnuson-Moss legislation of 1975, is an anomaly in this era of deregulation. The Commission has been historically an enforcement agency, not a regulatory agency in the accepted sense. The experiment in legislative rulemaking has not been a success, and it should be ended. The Magnuson-Moss authority converted FTC from an enforcement agency to a mini-legislature writing affirmative codes of business conduct for American industry. If rulemaking is to be preserved, at a minimum FTC's powers should be restricted to the issuance of rules which define unfair acts and practices with specificity, as now provided for in section 18 of the Federal Trade Commission Act. The ancillary authority contained in the Act to include in such rules affirmative requirements "prescribed for the purpose of preventing such acts or practices" should be eliminated. This is essentially a remedial power which should be exercised only in individual cases of violations where the remedy can be tailored to the particular facts.

UNFAIRNESS AND ADVERTISING

The proposal to eliminate unfairness as a basis for the regulation of advertising content is not a proposal for a radical change in the law. Indeed, I believe it would not change existing law at all. It would preserve intact the Commission's traditional authority over unfair methods of competition and unfair or deceptive acts or practices, which from the beginning has included undisputed authority over deceptive advertising. Its sole effect would be to restrict the Commission's unprecedented assertion of jurisdiction to regulate the content of non-deceptive advertising on grounds of unfairness.

This is an authority which the Commission has only recently claimed. It amounts to a general power of censorship over the content of commercial advertising because it is as broad as the broadest interpretation of the ill-defined word "unfair" in section 5 of the Federal Trade Commission Act. It is not necessary to speculate about the breadth of this power of censorship which the Commission claims to have found in section 5 because the Commission, its staff members and other advocates of an expansive interpretation have furnished us a number of guidelines and concrete examples.

The Commission claims that it has the power to regulate the content of non-deceptive advertising in order to advance broad, general concepts of public and social policy involving such imprecise objectives as the efficient functioning of free markets and an informed consuming public. It has repeatedly stated this view in its official pronouncements. For example, in the Commission's statement of the basis for its Trade Regulation Rule on insulation materials it said:

"The foregoing analysis is sufficient to support the Rule's provision for mandatory disclosure of R-values, because of the public policy favoring the existence and efficient functioning of free markets. A free market cannot function properly in the absence of effective competition which focuses on the merits and value of competing products and services. An essential element of effective competition is the availability of information that consumers need to evaluate competing products and to make the best possible choices."

The Commission couples this view of its powers under section 5 of the Federal Trade Commission Act with an expansive sense of mission as a business-reform agency. In issuing the so-called eyeglasses rule the Commission spoke of its affirmative "responsibility to promote the efficient functioning of markets," and then set forth the following definition of unfairness under the existing statute which would enable it to carry out its mission in just about any way it sees fit: The existence of competition is only one requisite for a functioning free market. There are a number of other factors involved such as availability of information, a lack of excessive transaction costs, a lack of costs incurred by or benefits accuring to persons external to the decision process, and mobility of resources. . . . Acts or practices which cause consumer injury by creating, exploiting, or *failing to alleviate market imperfections* other than a lack of or threat to competition can be unfair within the meaning of Section 5. (Exphasis added.)

Since, as economists tell us, in the real world all markets are imperfect, the FTC's view of the law gives it the power to impose on all advertisers its own economic and social views in requiring them to discharge their affirmative obligation under section 5 of the Federal Trade Commission Act to alleviate market imperfections. This opens a limitless regulatory vista for the application of a compulsory informational advertising program administered by the Commission.

Already the Commission has asserted that it has the power to compel a seller to advertise. The eyeglasses Rule stated that it was an unfair act or practice for sellers of opthalmic goods or services to fail to disseminate information, that is, to advertise, but then created an exception for a seller acting alone. However, in its explanatory statement it indicated that the creation of that exception was a discretionary act on its part. It asserted that a rule requiring the affirmative disclosure of information was "as action clearly within the Commission's power," but in the present case it did not need to use it and could rely on a less intrusive remedy. "It is not necessary to compel dissemination of information when simply permitting it is an adequate remedy," said the Commission.

Given the broad discretion granted the FTC in defining unfair practices under the statute, the agency has laid the groundwork for its exercise of an unprecedented power of censorship under its stated theories of unfairness in advertising. Some of the ways in which those theories might be applied have been hinted at in statements and proposals made by advocates of expansive FTC powers. For example, the 1978 FTC Staff Report on Television Advertising to Children described the advertising of breakfast cereals as unfair because, among other things, it was "distorting nutritional habits, negating what little nutrition takes place in the schools, and undermining the authority of parents in their own homes on matters of nutrition." The Staff wanted not only to regulate the content of such advertising but also advocated that the cereal manufacturers be required to fund a program of counter-advertising to be conducted by others.

Albert H. Kramer, until recently the Director of FTC's Bureau of Consumer Protection, has gone so far as to suggest that institutional, or "corporate-image" advertising, which does not convey product information at all, may be unfair advertising. In an interview published by the Bureau of National Affairs, Kramer said: "You are seeing a lot of ads that are directed at puffing up the company's image, at persuading the consumer to buy on the basis of an ad that is other than informational. It doesn't convey information, it doesn't make a direct claim; it attempts to convey an image of a product associated with a life-style or something of that sort. That's a little harder to get a handle on in traditional deception terms."

Speaking to the Washington Seminar of the American Association of Advertising Agencies in October 1980, Kramer returned to the same theme: "There are new trends and techniques emerging in the advertising industry which may pose difficult problems for the regulatory process. Corporate image advertising, designed to enhance the image of the company rather than to sell a product, exists now and is growing. One question there is whether consumers are likely to bring the same degree of skepticism to such advertising as they bring to traditional product ads. That is, are consumers more likely to be "taken in" by this technique and consequently less apt to question assertions made?"

The connection is simple to make. If advertising is unfair if it does not disclose the information customers need to make rational purchase decisions, then institutional advertising, which by definition does not convey such information, is by definition unfair. Furthermore, advertisers who attempt to persuade by the use of "emotional" rather than "rational" messages or associations, i.e., by the depiction of happy, smiling users of an advertised product, are also at risk of being charged with unfair advertising.

Serious advocacy of just such an application of section 5 was made in Reed and Coalson, "Eighteenth Century Legal Doctrine Meets Twentieth Century Marketing Techniques: FTC Regulation of Emotionally-Conditioning Advertising," 11 Georgia L. Rev. 733. Concerned that advertising may be based not on rational persuasion but on "emotional conditioning," the authors propose a basis for its regulation: "An advertisement becomes "unfair" under section 5 of the Federal Trade Commission Act as it portrays a product or service in proximity with (1) a dramatic display of emotional pleasure; or (2) the satisfaction of emotional needs or desires; or (3) the alleviation of emotional anxieties or fears, where such pleasure, satisfaction, or alleviation is substantially unlikely to be similarly engendered by the actual purchase or use of the product or product type. An advertisement also becomes "unfair" under section 5 as it portrays a failure to obtain the satisfaction of emotional needs or desires or portrays the creation of emotional anxieties or fears in proximity with an omission to purchase or use the advertised product or service, where such failure or creation is substantially unlikely to be similarly engendered by an actual failure to purchase or use the product or product type."

Can't you just imagine Canada Dry's lawyers trying to prove to an administrative law judge that ginger ale does, in fact, "taste like love?" These few example show just how broadly the concept of unfairness can be applied in regulating the content of non-deceptive advertising under FTC's existing interpretation of the law. Given the reluctance of the courts to interfere with FTC's "expert" determination of what constitutes an unfair practice within the meaning of section 5, it is clearly important for the Congress to clarify its intent in this case.

I do not believe that Congress intended to vest the Commission with the broad, affirmative powers of censorship over the content of commercial advertising that the Commission has claimed. A relatively simple amendment of section 5 to make clear that FTC shall have no authority to regulate the content of non-deceptive advertising on grounds of unfairness would take the agency out of the business of censorship while not diminishing its effective powers over false or misleading advertising and other unfair or deceptive trade practices.

Commercial advertising is a form of speech protected under the First Amendment. It is both good law and good policy that truthful, non-deceptive advertising employed to promote the sale of lawful goods and services in a free market should be free from governmental interference.

LEGISLATIVE RULEMAKING

During most of its long history, the Federal Trade Commission did not want, and did not think it had, the power to issue legislative rules, *i.e.*, rules defining unfair practices which would have binding effect on an industry-wide basis. In fact, it has generally been thought that an attempt to define unfair practices legislatively would be unwise, and Congress has frequently been hailed for its genius in refraining from making the attempt in the Federal Trade Commission Act and leaving the matter to be dealt with case-by-case in an adjudicative process. Typical of the many comments on the subject is the following classic observation by Justice Brandeis, quoted approvingly by the Federal Trade Commission itself in issuing its Trade Regulation Rule on Advertising of Opthalmic Goods and Services: "Instead of undertaking to define what practices should be deemed unfair, as had been done in earlier legislation, the act left the determination to the Commission. Experience with existing laws had taught that definition, being necessarily rigid, would prove embarrassing and, if rigorously applied, might involve great hardship. . . ."

Nevertheless, in passing the Magnuson-Moss Act, Congress gave FTC exactly such authority to issue legislation "which define with specificity acts or practices which are unfair or deceptive." Just as it was not a good idea for Congress to legislate specific definitions of unfair practices, it is no better an idea for the Commission to legislate such difinitions. What the Commission has, in fact, done under its rulemaking authority underscores the point. Its Rules are almost devoid of definitions of specific unfair practices, but full of mandated conduct. The Commission has recognized the impracticability of defining unfair practices and has chosen instead to formulate codes of compulsory practices, declaring that all other practices shall be deemed to be unfair.

The commission has been able to do this under the authority granted in the unobtrusive second sentence of section 18(a)(1)(B) of the FTC Act to include in its rules "requirements prescribed for the purpose of preventing such acts or practices." What this, in effect, has done is to convert the ostensible authority to write rules proscribing unfair practices into the authority to write codes of business conduct prescribing fair practices, similar to the infamous NRA codes of the 1930's. This similarity has been noted by others. When the United States Court of Appeals for the Second Circuit in 1980 set aside the Commission's Trade Regulation Rule on Proprietary Vocational and Home Study Schools, even the dissenting judge, who thought the rule was lawful under Magnuson-Moss, recognized it as an affirmative code of conduct and implicitly questioned the wisdom of granting such code-writing authority to an administrative agency: "The petitioners' major assault on the Rule . . . is that it ushers in a new era of N.R.A.-type industry-wide codes. That fear is not groundless. Whether codes of the type exemplified by the Rule challenged in this case are a sound way to protect consumers from misleading trade practices and whether the resulting burden of regulation is worth the benefits are policy issues for the Congress. When Congress gives an agency substantive rule-making authority, it accords it a large measure of legislative power. It is the responsibility of Congress to determine how wisely that power is being used." (*Katherine Gibbs School (Inc.) v. FTC*, 612 F.2d 658, 683.)

It has long been established that the Commission may include appropriate affirmative remedies in its cease and desist orders where necessary to prevent the continuation or recurrence of proven past violations in particular cases. But prescribing affirmative remedies on an industry-wide basis by rule is a far different matter. It places honest businessmen in the same straitjacket as the dishonest, and acts to suppress innovative competitive practices.

At a minimum, Congress should eliminate FTC's authority to include affirmative rules of conduct in trade regulation rules. But a better solution would be to eliminate substantive rulemaking altogether. The Magnuson-Moss experiment has not been a success. The proceedings have been interminable, and highly controversial. Covering excessively broad areas, they necessarily involve the participation of many different parties and interests and the accumulation of massive, well-nigh unmanageable records reflecting a bewildering variety of fact and opinion, much of it on highly subjective matters.

As the Special Project Report of the Administrative Conference of the United States emphasizes, the procedural aspects of FTC rulemaking have been a quagmire. The ill-defined unfairness doctrine "provides an extremely plastic, open-ended set of legal theories" upon the basis of which the Commission might proceed in any given case, creating a fundamental source of confusion and uncertainty for participants. In addition, the other two factors that FTC must address in Magnuson-Moss rulemaking—the prevalence of the practices and the economic effect of the proposed rule—are also sources of uncertainty because they are so subjective and controversial. As the Special Project Report says: "In short, all three of the statutory factors bearing on the ultimate decision can generate open-ended theoretical premises, and the range of potentially relevant argument and proof that can be adduced to support or attack those premises may be vast. As a result, different persons can have widely divergent perceptions of the issues of rulemaking. . . ."

It is inevitable, therefore, that legislative-type hearings in wide-ranging rulemaking proceedings will produce a proliferation of issues, plus extensive argument and evidence on all sides of every issue, as the numerous participants take the necessary care in their own interests to leave no possible basis of decision uncovered. Under those circumstances, virtually any final rule can be supported by rationale and substantial evidence found somewhere in the expansive record. The result was stated—or understated—in careful, diplomatic language, but with clarity of meaning, in the Special Project Report: "If the Commission remains free to frame broad and novel theories to support its rules, to decide issues on a best-estimate basis from an inconclusive record, and to rely on a wide variety of evidence to support its conclusions, then the procedural safeguards incorporated in the statute may seem fairly illusory."

Case-by-case adjudication is far more efficient and it gives better results. In a cease-and-desist proceeding, the FTC must still apply the subjective standard of unfairness, but it does so in the manageable context of a disciplined, adjudicatory proceeding devoted to the development of the facts relating to actual practices of a particular company in a particular market situation. Its findings and its prescribed remedy will be more limited in scope, and more likely on target, than its legislative pronouncements in an industry-wide rulemaking.

A cease-and-desist order in an adjudicated case will not have the negative and undesirable side effect which industry-wide rules can have of restricting the inoffensive or innovative practices of honest sellers. Nevertheless, under section 5(m) of the FTC Act, the Commission's definition of specific practices as unfair in a individual adjudicated case is binding on an industry-wide basis, exactly as in a trade regulation rule.

In 1973 the Congress added a new section 13(b) to the Federal Trade Commission Act which authorized the Commission to seek a court-issued injunction to halt immediately a suspected unfair practice pending FTC's issuance and adjudication of an unfair-practice complaint under section 5(b) of the Act. No such immediate relief is available in the case of rulemaking.

Adjudicated cases, being narrower in scope and more specific in subject matter, should not take as long to complete, on average, as the drawn-out, controversial rulemaking proceedings which, the record shows, linger for years at the Commission. Furthermore, the pre-complaint investigation in an individual case should be concluded much more promptly than the years-long, industry-wide staff studies which now often precede rulemaking. Consent orders, which have been used effectively by FTC and other agencies, eliminate the need for any type of hearing procedure and are, therefore, very efficient, but they have no practical counterpart in rulemaking.

Former Commissioner Robert Pitofsky, addressing the ABA's National Conference on Federal Regulation in Washington in September 1979, emphasized the changing nature of rulemaking at the FTC by contrasting the broad scope and complexity of the TRR's of the late 60's to the narrowed scope of the more recent rules in which, he said, the Commission has opted for emphasis on one or two central matters rather than try to cover the numerous matters which its staff might have originally proposed. This is particularly interesting because, of course, as a rule becomes narrower in focus it begins more and more to resemble a cease-and-desist order, and whatever theoretical justification might have been thought to exist for preferring rulemaking to adjudication disappears.

The elimination of FTC's rulemaking authority will improve its efficiency and effectiveness, and conserve its scarce resources. Given the lack of evidence disclosing significant benefit from the rulemaking experiment, I urge that it be abandoned.

[The following information was subsequently received for the record:]

Brown & Williamson Tobacco Corp.,
Louisville, Ky., March 29, 1982.

Hon. Wendell H. Ford,
Russell Senate Office Building,
Washington, D.C.

Dear Senator Ford: Your question "Should the FTC have authority under the standard of 'unfairness' to deal with the issue of any dental health hazards of sugared cereals" is related to the line of questioning Senator Packwood posed to members of the advertising industry on the subject of dental-health hazards from pre-sweetened breakfast cereals. I have no credentials as an expert in either cereal products or dental health. I do have a deep concern, however, about the disconcerting precedent that would be established by Congressional acquiescence in the FTC's asserted power to regulate non-deceptive advertising of such products for public-health purposes. As you know, FTC has asserted such authority under its so-called "unfairness" jurisdiction.

It seems to me your question implicates another agency, the Food & Drug Administration. Unless I am missing something, the food additive provisions of the Federal Food, Drug and Cosmetic Act render unlawful any use of a food additive unless its use conforms to either an experimental exemption or a regulation prescribing the conditions under which such additive may be safely used. Such conditions of safe use expressly include specifications by FDA as to the maximum quantity which may be used or permitted to remain in or on any particular food. In this regard I am thinking of 21 USC Section 348, a statutory directive that would seem to be clearly applicable to the addition of sugar to breakfast-cereal products.

FDA, however, has chosen to exempt sugar from any food additive controls by continuing to carry it on its GRAS list—"Generally Recognized As Safe". Ironically, various groups who supported FTC's "kid-vid" rulemaking apparently thought the use of sugar in pre-sweetened cereals is generally recognized as hazardous. Indeed, on December 19, 1977, the Commissioner of Food and Drugs wrote the Chairman of the FTC urging the FTC to regulate the advertising of sugared food products, citing an FDA-sponsored scientific study which concluded: Reasonable evidence exists that sucrose is a contributor to the formation of dental caries when used at the levels that are now current and in the manner now practiced.

"Little doubt exists", the Commissioner added, "that excess sugar in the diet contributes to dental caries". How, on that record, can the FDA justify its action in continuing to exempt sugar entirely from regulation as a food additive when it believes that its excessive use in prepared foods is hazardous to dental health? And what sense does it make to try to protect the public health by regulating the non-deceptive advertising of sugared foods when neglected law already on the books permits the manufacture of such foods to be regulated directly? More to point, should advertising space be commandeered by any agency to carry a nutritional-education message unless Congress clearly grants it proper authority?

I think it is a poor idea to allow a trade regulation agency, with no relevant expertise, to stretch its trade practice authority to cover regulation for public-health or other open-ended public interest or public policy purpose with no more guidance than provided by the "unfairness" standard.

In urging that FTC be denied the authority to censor non-deceptive advertising on the vague and potentially all-encompassing grounds of "unfairness", I am not advocating reduced consumer protection, nor do I think that would be the result. The true purpose and effect of the carefully limited proposal to prohibit the regulation of the content of non-deceptive advertising on such grounds is to prevent the Commission from engaging in censorship of free commercial speech.

[The following information was subsequently received for the record:]

Brown & Williamson Tobacco Corp.,
Louisville, Ky., April 20, 1982.

Hon. Robert W. Kasten, Jr.,
Chairman, Senate Consumer Subcommittee, Russel Senate Office Building, Washington, D.C.

Dear Chariman Kasten: This letter is written to follow up the "fairness doctrine" testimony, which you kindly allowed me to present for this Company and for our affiliated companies Gimbels, Saks Fifth Avenue and the Kohl stores, before the Senate Consumer Subcommittee on March 19, 1982.

For fear that the more spectacular attention given to Chairman Miller's controversial proposals will cause the central issue relating to fairness to be shunted aside, we wish to stress the advantages of our limited proposal for amendment of the Federal Trade Commission Act. Its sole purpose is to prohibit FTC's regulation of the content of non-deceptive advertising on ill-defined grounds of unfairness. This proposal is a measured response to a demonstrated need, which takes up where the Committee left off in 1980 when it imposed such a limitation on the Commission's authority in rulemaking.

Chairman Miller's proposal on the subject of unfairness, which he has referred to as a "definition" of unfairness, is not truly a definition, and it does not address the problem of concern to advertisers. That concern, extensively documented in testimony before the Committee, is that the censorship authority which inheres in such a vague word as "unfair" is virtually boundless.

The Chairman's three-part legislative proposal—substantial injury, not outweighed by contervailing benefits, and not reasonably avoidable—defines injury, rather than unfairness. It is, as characterized in his letter to you of March 5, 1982, a definition of the "basic elements for evaluating consumer injury" from a challenged trade practice. It deals only with the evidence of injury appropriate to sustain an unfair-practice charge. It says nothing about the nature of the unfair practice itself. The existing concepts of unfairness in advertising which have been enunciated by the Commission and its staff would be unaffected. As the Chairman's March 5 letter stated, the proposal merely codifies existing Commission practice.

The proposal I urge the Committee to consider is a simple, carefully circumscribed amendment of Section 5(a)(1) of the Federal Trade Commission Act. It is designed to accomplish the single objective of prohibiting the Commission from regulating in either adjudication or rulemaking the content of non-deceptive advertising on the grounds that it appears to the Commission to be somehow unfair. the proposed amendment would add the following sentence at the end of Section 5(a)(1) of the Act:

"Unfair methods of competition and unfair or deceptive acts or practices shall be deemed to include the use or dissemination, or causing the use of dissemination, of advertising only to the extent that such advertising is false or deceptive."

The language has been carefully coordinated with the existing language of Section 5 and does not introduce arbitrary distinctions among the concepts of unfair methods of competition, unfair acts or practices, and deceptive acts or practices for which there is no precedent in the history of the interpretation of the Act. After all, the prohibition of false advertising was not introduced by the Wheeler-Lea Amendment in 1938. Among the earliest decisions under the original 1914 Act were holdings that the dissemination of false advertising was an unfair method of competition.

The language of the proposed amendment has also been coordinated with the language of Section 12(b) of the Federal Trade Commission Act, which also deals with advertising and says:

"The dissemination or the causing to be disseminated of any false advertisement within the provisions of subsection (a) of this section shall be an unfair or deceptive act or practice in or affecting commerce within the meaning of section 5."

Preserving consistency in the language and structure of the Act avoids introducing the uncertainty associated with the use of language and forms for which there is no precendent in the prior history of the interpretation of the Act. For example, if the Chairman's proposal were accepted as a "definition" applicable to unfairness but not to deception, as seems to be the intent, would it become necessary in each case to decide whether a challenged practice was an unfair or a deceptive practice, and to proceed in reliance upon one legal theory or the other at the risk that a court might later disagree with the classification? Or would it become virtually mandatory to use both concepts, unfair and deceptive, and meet the Chairman's proposed new legal tests for both?

I do not see how such uncertainty, and technicality, can serve the interests of either the Commission or the businesses it regulates. As I said in my statement, I also am not aware of serious problems associated with the Commission's exercise of its unfairness authority over non-advertising practices, so I do not see the need to attempt to redefine the term "unfair", a difficult task, at best, with clearly unpredictable consequences.

However, the proposal I suggest is not in conflict with the proposed "definition" of unfairness put forward by Chairman Miller. I urge adoption of my proposal in any event, without regard to any action that may be taken on the Chairman's proposal.

Sincerely yours,

ERNEST PEPPLES.

Senator KASTEN. Thank you.

Senator Packwood.

The CHAIRMAN. Mr. Rogal, do I understand your testimony to be that all truthful advertising is necessarily nondeceptive?

Mr. ROGAL. Truthful advertising——

The CHAIRMAN. Ipso facto is nondeceptive.

Mr. ROGAL. Well, of course, there is the element of the truthful ad which could be misleading by omission. Is that what you are referring to?

The CHAIRMAN. I am looking at your statement where you talk about the Supreme Court's decision in Hudson Gas: "The first test is to initially determine whether the advertising is true or false. If it is false, that ends the matter for false advertising is not protected by the First Amendment in our opinion. If the advertising is true, i.e, nondeceptive, that should also end the matter."

Do I take it from that statement that you are saying that all true advertising is nondeceptive?

Mr. ROGAL. No; I do not mean that by that, but explaining the statement, I just meant that if the advertising is truthful and nondeceptive, the Government should have no power to interdict.

The CHAIRMAN. Truthful and nondeceptive—so you can have advertising that is deceptive and is true?

Mr. ROGAL. Possibly. It can be deceptive by omission.

The **Chairman**. It can be deceptive in a number of ways, but I want to make sure that you are not maintaining the position that all true advertising is ipso facto nondeceptive.

Mr. **Rogal**. No; we are not maintaining that.

The **Chairman**. OK. You are saying that we should have the right to regulate advertising if it is false or deceptive.

Mr. **Rogal**. That is right.

The **Chairman**. OK. Now, we had a long battle over children's television, and you have made reference to it in your testimony. I take it your position must have been that the advertisement of heavily sugared products to children was, first, true, and second, not deceptive.

Mr. **Rogal**. That is correct.

The **Chairman**. And therefore, if those two standards are met, there should be no reason to regulate such advertising even though from a health standpoint it was harmful to children.

Mr. **Rogal**. We do not agree, of course, that it was harmful to children. These are sugared products that have been on the market for many years. They are generally recognized as safe, and we just felt that under those circumstances, you should be able to advertise it truthfully without deception. You should not advertise it as being an aid to dental health.

The **Chairman**. You are not advertising it as being an aid to dental health?

Mr. **Rogal**. I do not believe that you could do that with a candy bar or a product of that kind.

The **Chairman**. But you think it is no harm to dental health.

Mr. **Rogal**. That it is no harm to dental health?

The **Chairman**. Yes; that candy bars and sugared cereals are no harm to dental health.

Mr. **Rogal**. I do not believe they harm children's health at all.

The **Chairman**. Is there any respectable evidence in the academic community that reaches a different decision?

Mr. **Rogal**. There is in the rulemaking record, file cabinets full of studies as to what has happened with respect to dental health since television advertising started. It has gone down, and——

The **Chairman**. Let me back up. Are there any studies by the American Dental Association that indicate heavily sugared foods or candy bars are adverse to children's dental health?

Mr. **Rogal**. I am sure there must be.

The **Chairman**. There are.

Mr. **Rogal**. I am sure there must be. Of course, the view of the industry is that when sugared products are used properly, and children use proper dental health procedure, brush their teeth, that they do not do harm.

The **Chairman**. That is not even the conclusion of the American Dental Association. I do not know of any dental report in the last 20 years or any medical report that is even neutral as far as heavy use of heavily sugared products is concerned.

Mr. **Rogal**. Well, I must admit that I do not recall all of the studies extant in that record, but I do know that the industry presented many, many studies of its own, and the record was not entirely clear one way or another on this factual question. I suppose that the advocates on both sides argue that their evidence supports their views, as usually happens in a factual controversy.

Mr. **Weil**. I gather the implication of your questions is that if our proposal to remove commercial speech from the coverage of unfairness were adopted, that then the Commission would be left with no remedy against advertising to children that could harm their health in connection with sugared products. Let me make two comments on that, if I may:

No. 1, if in fact the proof, the evidence is strong enough that there is a health harm in connection with such products, the Food and Drug Administration can bar them from the market as unlawful food additives.

No. 2, even the Commission would not be without weapons, because under section 15 of the Federal Trade Commission Act, an advertisement of a food, drug, cosmetic, device which fails to point out harmful or other undesirable consequences of using that product is explicitly defined as being misleading and deceptive. So, the FTC could move even in that circumstance without having to rely on unfairness.

The **Chairman**. Is it the position of Mr. Rogal and yourself and the organizations you represent that heavily sugared foods and candy bars are not adverse to the dental health of children?

Mr. **Weil**. Well, speaking for myself, not for my association—we have not discussed this—but for myself and with some familiarity with these proceedings, I would say that at the present the evidence leaves it on the standing of a scotch verdict of not proven and not disproven.

The **Chairman**. Yes, sir, Mr. Versfelt.

Mr. **Versfelt**. I would endorse Mr. Weil's last comment. We are not here as experts in the dental health field, and I would want to be very careful not to make any assertions one way or another on the complicated factual merits that came up in the children's advertising proceeding.

I would like to add, however, that as your questions brought out, Senator, the Commission, had it gone forward after the Improvements Act with the children's advertising proceedings on a theory of deception, would have had a crack at going after advertisements of the kind you described. They chose not do to so. In our opinion, the authority to move under classic principles of deception should be sufficient for the Commission.

The **Chairman**. You are missing my question. I just want to know if the three of you are contending that the evidence on the effect of heavily sugared foods on children's dental health is not yet in, and that therefore we do not need to address the question of fairness or unfairness or deception, because you do not even have a factual determination as to whether there is any danger.

Mr. **Versfelt**. I am not making that assertion, Senator.

The **Chairman**. I think that is what Mr. Weil said.

Mr. **Weil**. That is my personal position.

The **Chairman**. Mr. Rogal.

Mr. **Rogal**. As I stated, I have not reviewed that record with the kind of detail that would be necessary if I were sitting as a judge to decide, but it seems to me that it is almost ridiculous to state that any product that has sugar in it is harmful to health. There are so many. There is ice cream, there is candy, there is chewing gum, there is sugared cereals. In the case of sugared cereals, there may even be less sugar there than the child typically puts on it himself, and where do you stop with this kind of unfairness rationale?

There may be a host of other products out there on the market. Alcoholic beverages will get you drunk. Do you have to disclose all of that sort of thing?

Senator **Ford**. Be careful.

Mr. **Rogal**. There is no place you can stop if the Federal Trade Commission is empowered to do this type of thing.

The **Chairman**. My time has run out. I will come back to you.

Senator **Kasten**. Senator Ford.

Senator **Ford**. I was interested in listening to the chairman. I am almost willing to give up my time.

For the panel, what advertising cases have been brought strictly under unfairness in section 5, and would the Commission be unable to bring certain cases that it brought in the past if unfairness is eliminated as a basis for case-by-case adjudication under Section 5?

Mr. **Versfelt**. Senator, if I could go first, to my knowledge, there have been no ad cases brought by the Commission exclusively under the unfairness jurisdiction, unfair acts or practices. Nothing comes to mind in a sense that would leave the Commission without authority to move in a case-by-case manner, if the unfairness jurisdiction is amended as by our proposal.

To my knowledge, every adjudication that has gone to ultimate determination has been based by the Commission at one point or another on both unfairness and deception or else on deception alone.

Senator **Ford**. Does anybody else care to respond?

Mr. **Weil**. Senator Ford, may I have it understood that my comments are limited entirely to the area of commercial speech? I am not talking about other acts or practices.

Senator **Ford**. That was my question, Mr. Weil.

Mr. **Weil**. Yes. I am familiar with one case, because I have been counsel in it, where a major aspect—it has not been decided yet. It is pending for decision before the Commission right now, but a major aspect of it, it was a pharmaceutical case, in which certain comparative claims were made in the advertising for superiority of the advertised product over others, and a major aspect of that was stated by trial counsel for the Commission and prosecuted by them on the theory that they did not care whether the claim was true. The claim could be perfectly truthful, and indeed could be supported by some reasonable basis other than the particular type of scientific proof that they were insisting upon.

And that, I might say, was a scale of proof which in many respects went far beyond for an over-the-counter product what the Food and Drug Administration itself requires in order to approve a new drug prescription, a new drug, prescription drug, and this is what trial counsel were insisting upon, purely on the basis of unfairness.

Now, we have heard, similar to your question, Senator, "Well, has the FTC ever done any of these horrible things in the final showdown, the final cease and desist order that was upheld by the courts?" Perhaps not as yet, but if the Commission has not bitten, it has certainly growled and snarled, and that has a chilling effect.

There are many, as you know, small- and medium-sized businesses which can be chilled away from engaging in activities which lawfully they may have a right to follow because the Commission has issued some complaints and gotten consent orders or has issued guidelines or by other forms, other modes, it has made it known that it considers certain activities unfair, even though truthful, and businesses of that kind and even large businesses, where they feel that the claim is not worth a candle of fighting and maybe having to go all the way up to the Supreme Court, will withdraw it rather than face such litigation.

Now, an important aspect that the courts emphasized, in connection with first amendment protection; it is if anything even more for the benefit of the recipient, of the listener to get the information than it is for the benefit of the speaker to utter it, so that both the business and the consumer are harmed when these chilling effects take place, which are really not deserved, because they may be asserted under a part of the statute which under first amendment principles cannot back them up.

Mr. **Greenberg**. I have a couple of comments, Senator Ford.

Time and time again the Commissioners themselves have said that there are many cases whether or not they are in a sense pleaded in the alternative containing both theories that they feel would stretch the definition of deception far beyond any meaningful phrase in order to make their case.

Senator **Ford**. Can you name the case?

Mr. **Greenberg**. Well——

Senator **Ford**. A case?

Mr. **Greenberg**. Well, let's take an example of rulemaking, the insulation rule, where they were required to disclose the R value, which in and of itself, it is very hard to argue that the failure to disclose that fact is inherently deceptive, and let's also take the same, I believe it is the *Meco* case, which showed a child playing with an electrical appliance near water. It is very hard to make a case that that is inherently deceptive. What is deceptive about that?

The fact of the matter is, though, that that sort of showing can induce imitation behavior. It can say that that sort of activity appears to be acceptable behavior, but a broader comment on all this is that if what the gentlemen for the advertising industry are seeking is clearer standards, and that seems to me to be what they are saying to us today, they are not saying that cases should not be brought, they are saying that legitimate cases can all be captured under the rubrick of deception, which is basically then just a question of, do we have appropriate standards? The Commission has provided those standards. It seems to me that the rest of industry has been willing to accept those standards and live by those standards, although we have an argument about whether or not they should be codified.

No one else is asking for a complete exemption from those standards, and I think that if what we are talking about is the actual merits of cases and whether we have appropriate standards for the

Commission to act under, then we have them, and we should get away from talking about total exemption for one industry.

Mr. **Rogal**. May I jump in on that? This R value thing has been thrown out two or three times. In our opinion, if that is based upon unfairness, that is a typical example of abuse. If you have to use the required disclosure that the Commission had dictated, it would take up at least 16 to 17 seconds of your 28-second commercial, leaving the advertiser with 14, 15 seconds, or something of that nature to present his product.

As with the *Mego* case, I believe that that case could clearly be brought under a deception theory. The Commission charged that this advertising has the capacity and tendency to induce children to do something dangerous. Well, it seems to me that what they are saying here is that it has the capacity and tendency to mislead children into performing a dangerous act, and it could clearly be reached, and I cannot conceive that a court in a case where the safety of children is involved is going to overrule the Commission and say, hey, when you had unfairness authority it might have been OK, but this is not deception. I just do not believe that would happen in the real world.

Senator **Ford**. So to protect the safety of children, this could come under deception?

Mr. **Rogal**. Of course, sir. As a matter of fact, as I pointed out, they charged it under all three. They charged that it was an unfair method of competition, they charged that it was deceptive, and they charged that it was unfair. That is what the complaints read, and that is all we have, are the complaints in the order.

Senator **Ford**. Let me ask one quick question then for the panel. Yesterday Chairman Miller suggested that deceptive acts or practices should be further defined. Do you believe this is necessary?

Mr. **Rogal**. Senator, we recognize that the Commission has in many instances brought a lot of trivial cases, cases in which it probably was a waste of the public money and which probably performed no good for either the public or competition, and we are greatly encouraged by his view that something should be done in that category, and as we stated, we are going to look into that and submit a later statement for the record.

Senator **Ford**. Does anybody else on the panel have a statement? Mr. Greenberg.

Mr. **Greenberg**. Yes, Senator, we are very pleased by the Commission's statement contained in the letter to Congress in December of 1980 where they set out their own internal standards for insuring that their resources are used in a way that will benefit the most consumers and the most competitors, and we feel that that sort of definition is entirely appropriate, and do not feel that it should be set in concrete by legislation which we think will only lead to litigation over each individual term.

Senator **Ford**. Mr. Pepples.

Mr. **Pepples**. Well, I know that Senator Exon was an attorney general at one time, and I hesitate——

Senator **Exon**. I wish to correct you on that, Mr. Pepples. One of my great claims to fame is that I am not a member of a bar.

Mr. **Pepples**. I know there is one other colleague——

Senator **Exon**. Let's correct the record on that.

Senator **Ford**. We have two on the committee, Mr. Pepples.

Senator **Exon**. That will apply to almost everyone else.

Senator **Ford**. Senator Gorton.

Mr. **Pepples**. I have spent 20 years trying to understand the statutes that you enact and the ones that other bodies enact, and I am inclined to be slow about looking for new wording and new phrases, particularly when you have a statute that has been around as long as the FTC act has. I would be somewhat slow, I think, in following the suggestion that this unfairness definition be put in the statute. It is just an exhortation to use good sense, and I am concerned about the ability of the Congress to successfully legislate good sense into anybody's head.

It is certainly encouraging to hear a Chairman of the Federal Trade Commission indicating the standards that he would like to see involved in making these important decisions about which cases to bring. But it is like a prosecutor bringing a case. There are a lot of things that he should think about, and I think that just his good judgment probably is the best thing to rely on in this sort of a situation rather than encumbering a statute with a lot of rubbery language. I am relying on the Washington Post description of the definiction in the paper this morning. I did not attend yesterday's hearing. I did read the March 5 letter to Chairman Packwood and Chairman Kasten, and I believe that is the same language that is being proposed as the statutory change, but it would trouble me to see that language brought into the statute.

Mr. **Versfelt**. At the risk of going on too long with this, I know that the American Association of Advertising Agencies commends the Chairman of the Federal Trade Commission for coming down to the committee yesterday and speaking so candidly about what he sees as the costs and benefits of the deceptiveness standard.

We will, as Mr. Rogal said, look into that standard and be willing to work with the committee in any way it wishes. Our principal contention this morning, however, is that it is the unfairness jurisdiction of the Federal Trade Commission that is in essence undefinable; that is, therefore, of immeasurable bounds; and that has throughout the aggressive years of Commission activity in the 1970's led to attempts at rulemaking on, essentially, the whims of the Commission staff.

It is our position that because commercial speech takes place in an area of first amendment overtones, of constitutional protections, that it is the unfairness jurisdiction that should be addressed by this committee.

Senator **Kasten**. Senator Exon.

Senator **Exon**. Thank you, Mr. Chairman. This is a point I wanted to follow up on. I would first like to make a statement on my position on this, and then have any member of the panel that wishes, make a response. Just about the time, gentlemen, that my strictly business background indicates to me that the Federal Government is becoming too much involved in business affairs, and since in my office, with the possible exception of balancing the budget and doing something about the low level of prices that we see in the farm economy today, the overall regulation of business probably generates more mail and controversy than anything else.

I am aware of what you are talking about and just about the time, with that background, I feel by golly, it is about time we do something up here. Then just about that time, I see a commercial speech on television that flips me and says we had better be awfully careful about what we do, even though I wholeheartedly agree that there has been cases upon cases where the Federal Trade Commission has gone what I think was beyond what was intended in the law. And in addition to that, beyond good judgment.

So, with particular regard to advertising, commercial speech, truth in advertising, deception and unfairness, I would direct the attention of you people in the advertising business that I see such things on television and I have seen them within the last 90 days. And I do not watch television very much.

I have seen such things as the old, wornout fire sale, going-out-of-business sale, only more so. I have seen advertisements that sell portraits or original paintings—come to the motel and see them. And one that I thought was the most humorous of all was the prior-to-bankruptcy sale. Get in on this big deal before bankruptcy. I had never seen that used before. I think it is deceptive, I think it is unfair, I think it is misleading.

I have also seen very recently an ad where senior citizens can buy life and health and accident insurance, and lo and behold, they get all these wonderful benefits. But what is featured over and over again on that commercial ad is that the policy cannot be canceled. Marvelous thing.

I have also seen—and usually those types of things in commercial speech features someone who is easily identifiable like a movie star or a television personality or someone that the people have come to trust because of their previous exposure. One other one featuring a well-known movie star is a special veteran's life and health and accident insurance policy for veterans only, those who served the country in time of need.

I am only saying this to you because this is a major concern to me in my long service in the public in recognizing that the only reason we have these laws is that business and advertising have abused people in the past. Otherwise, we would not have these laws. And we would not be meeting here today to try to address some of the overactions or reactions of Government to the laws that have been passed by the Congress.

Let me ask this question of you people in the advertising business. Do you have any kind of a self-policing agency, a commission or anything else, that tries to judge what is proper and what is not proper in the way of self-policing?

Mr. WEIL. Indeed, we have, Senator. And I might say that your concern is not only shared by the responsible advertising and advertising agency associations and their members, but we feel that, if anything, even more intensely because there is no point of making the vast expenditures for advertising that are made if it cannot command credibility.

Now, there is an operation of the council of better business bureaus known as the National Advertising Division, which does police advertising, which receives complaints that anybody would want to send in, whether a competitor or a consumer or some member of some government. It does not matter. When those complaints are received, they are thoroughly investigated. The advertiser involved is called upon to present substantiating evidence for whatever claim has been challenged.

If the National Advertising Division decides that the claim is not properly substantiated or is even untrue, it calls upon the advertiser to correct it. If the advertiser refuses, then the NAD, not being a governmental organization, cannot enforce but it will bring the matter to appropriate governmental agencies that can enforce, including State's attorney generals, including the Federal Trade Commission, including the Postal Service, including Food and Drug Administration where that would be an appropriate policeman for that particular product, those particular claims. So, indeed, the advertising industry does do everything it can to keep its act clean.

Now, I was interested in the examples you gave, Senator. I would say 90, if not close to 100 percent of them were local advertising. It is very difficult for the advertising industry to control these local things, the used-car dealers, the very types—the going-out-of-business sales. These are all local things.

Insurance is probably the only one that would go across national or regional lines, and I am not sure but I think the Federal Trade Commission has no jurisdiction over insurance. I think that is left to the States for regulation, and to the State superintendents of insurance.

To respond to what you are really getting at, Senator, yes, indeed, we are very concerned about any untruthful activities, and our proposal does not contain any hint of wanting to diminish in any way the Federal Trade Commission's control over misleading advertising.

Senator EXON. I thank you for your question. I am glad to know that you have such an operation.

I would simply say that regardless of whose responsibility it is to enforce when we are talking about the advertising agency, the studio, the people that go to put this together, for the most part I suggest that they are not fly-by-night operations. Now, they may be, some of them.

Mr. WEIL. That is right.

Senator EXON. But I would hope you could do a better job in the future than it has been my perception that you have done in the past. Thanks for trying.

Mr. WEIL. Thank you for your comments, Senator.

Senator KASTEN. Mr. Greenberg, we will ask you to respond to that same question.

Senator FORD. Could I get involved here just a minute? The NARB has had good voluntarily compliance, as I understand.

Mr. WEIL. Excellent.

Senator FORD. I think you are to be complimented on that. And I think it is the philosophy of the present administration that you do that sort of thing and keep the Federal Government out.

It seems to me there is a recent case that indicated there might be an antitrust violation where you are coming together to make this decision.

Mr. WEIL. I think the antitrust aspect of that case was reversed.

Senator FORD. Was it reversed?

Mr. Rogal. I believe you might be speaking of the NAB, the *National Association of Broadcasters* case, which was recently in the paper, their self-regulation effort.

The difference, if difference there be, between our self-regulatory efforts as far as the antitrust laws are concerned is that we have no policing arms, we have no ability to enforce, and therefore, we only go to the Federal Trade Commission or to a State agency to enforce. In other words, it is a persuasive type of thing.

I might also add that the American Advertising Federation, Senator Exon, is extending the self-regulation to the grassroots.

Senator Kasten. Mr. Greenberg, do you want to make a brief comment, please?

Mr. Greenberg. Yes. My comment is almost implicit in Senator Ford's remarks. The single greatest damage that Congress could do to, in many cases, the laudable, voluntary efforts of the advertising industry would be to cut back on the FTC, because you can hinge the voluntary effort of this industry, and almost all other industries, to effective Government power and Government standing at the sidelines.

Senator Ford. I think it is Baltimore that fined a local merchant for a going-out-of-business sale.

I might say that the FTC does have control over insurance companies' advertising.

Senator Kasten. Mr. Versfelt, it seems to me that the question which we have not focused on enough is the uncertainty inherent in how to define "unfairness." One person or one group of Commissioners could think something unfair that another group would think was not unfair. So isn't uncertainty about how the law will be applied part of the problem with the application of the unfairness authority to commercial advertising?

Mr. Versfelt. Indeed it is, Senator. I think that the uncertainty that adheres in an essentially undefinable term like unfairness gets reflected within the Commission, as I think we heard this morning from a member of the earlier panel, and also gets reflected outside of the Commission.

With the Commission, over time, not having any idea or not being able to have any idea of what the notion of unfairness means, it is unable to give adequate directions to its staff; it is unable to decide before a rulemaking proceeding or an adjudication begins whether the initiative is something that is proper for the FTC to undertake; and it is unable ultimately to make decisions once those trade regulations, rulemakings, or adjudications come before it for final determination.

Senator Kasten. Is there any way you can define or quantify the cost to the industry and indirectly to consumers of this uncertainty and the legal problems it might create? I am not in the advertising business.

Mr. Versfelt. I suppose, Senator, it is probably impossible to come up with a definite figure, a dollar amount. But I think the costs, it is safe to say, are immense. I noticed in one of the submissions from yesterday that the dollar cost estimated for simply the industry's response in the children's advertising rulemaking—was about $35 million over the years—and that leaves out the Government's—the taxpayers'—direct costs.

In addition, there are nonmonetary costs of substantial size that Mr. Weil alluded to earlier, and the chilling effect in the area of first amendment concerns when people outside the Commission cannot foresee what, in advertising, is going to be considered appropriate and what is going to be considered unfair some day down the road. There are a lot of good ads that do not get made.

Senator KASTEN. Mr. Rogal, what is your view of the advertising substantiation doctrine? Would that be preserved under the proposal that you have brought before us today?

Mr. ROGAL. Yes, sir. First, as to the view of it, we certainly, I believe, all of our associations and members of our associations, are agreed that the advertising substantiation doctrine should be preserved and should not be affected in any way. It is our belief that a person who makes a positive claim in an advertisement such as some that have been spoken of here today, if he says 9 out of 10 persons prefer—a statement like that clearly implies to the consumer this fellow has conducted some kind of study; he has some kind of evidence, he has something. Otherwise, he could not have made such a statement, 9 out of 10.

And if he does not have that evidence, we feel it can be reached under the deception standard. I might refer you to a case the Commission brought, when it first——

Senator KASTEN. I think, Mr. Rogal, I am going to interrupt and ask you to submit the case and that data to us for the record.

Mr. ROGAL. I just want to correct the record. We started the local advertising review board program some time ago and it is now in place in about five or six cities, and we hope to expand it.

Senator KASTEN. Senator Ford, Senator Exon? No questions?

Thank you, gentlemen, for your participation this morning. We appreciate your help. The next panel is made of Mr. Roush, Mr. Gressman, Mr. Morrison, and Mr. Angoff.

This panel is on the question of legislative veto, a controversial subject of great interest to me and other committee members. The FTC Improvements Act of 1980 established a new procedure for congressional review of newly promulgated FTC rules. Under this procedure, a rule would take effect unless it is disapproved by both Houses of Congress within a 90-day period. This veto provision expires at the end of the current authorization, on September 30 of this year, so it must be extended if it is to remain effective.

Since the Improvements Act was passed, only two rules have been promulgated by the FTC and submitted under the veto provision. The first was a noncontroversial amendment to the FTC's games of chance rule that simply waited out its statutory review time uneventfully.

The second submission, the used-car rule, has proved more controversial. The rule was promulgated by the Commission in August and submitted to Congress in September. Following a consumer subcommittee hearing, the committee voted 12 to 4 to report Senator Pressler's disapproval resolution to the Senate.

When the Senate was unable to consider the issue before adjournment, the issue was put over until this session. I expect the committee will consider the new disapproval resolution soon, and that the House and the Senate will ultimately disapprove this rule.

While the process is not yet complete, I believe our experience with the used-car rule illustrates how well congressional review of agency rules can operate in practice. I have long been a proponent of legislative veto as a means of controlling bureaucratic excesses, and I would like to see the FTC legislative veto extended. And I might add that I am openminded about suggested alterations to the veto statute. We have come a long way since the Improvements Act was passed, based on our experience with the used-car rule and based on the work of Senator Schmitt and others who have worked on this issue in the context of the regulatory reform bill. I intend to work closely with Senator Schmitt and others to improve and to streamline the process.

Gentlemen, we look forward to hearing your thoughts on this important issue. And the first statement will be from Michael Roush.

STATEMENTS OF MICHAEL O. ROUSH, LEGISLATIVE REPRESENTATIVE, NATIONAL FEDERATION OF INDEPENDENT BUSINESS; PROF. EUGENE GRESSMAN, UNIVERSITY OF NORTH CAROLINA, SCHOOL OF LAW; ALAN MORRISON, DIRECTOR, PUBLIC CITIZENS LITIGATION GROUP; AND JAY ANGOFF, CONGRESS WATCH

Mr. Roush. Thank you, Mr. Chairman. My name is Mike Roush, I am a legislative representative of the National Federation of Independent Business, and it is a pleasure to be able to present the views of our 500,000 small business owner/members on the issue of legislative veto.

My oral statement is extremely brief, but I would like my written statement to be put in the record if possible.

Senator Kasten. Without objection, so ordered.

Mr. Roush. The NFIB urges this committee to include a legislative veto provision in its reauthorization bill for the Federal Trade Commission when it reports such a bill to the full Senate.

Our members and indeed, the whole small business community regard legislative review and possible veto of proposed agency rules as a necessary and entirely appropriate role for the Congress in exercising its lawmaking authority. Small business people view the issue as primarily one of accountability. That is, they elect Congressmen and Senators to write their laws, not hired or appointed civil servants. And while Congress may delegate part of its authority to agencies like the FTC, it cannot delegate its responsibility to the people.

Small business people regard rulemaking as lawmaking, and therefore, strongly believe that Congress should procedurally be able to review and, if necessary, block regulations before they go into effect with the force of law. To them, it appears not only constitutional but logical and reasonable, as well as simple and direct.

We regard suggestions that Congress delay action on legislative veto proposals because the Supreme Court may decide it is unconstitutional as strategems and not arguments.

As to the form of legislative veto to be included in the FTC reauthorization bill, NFIB would like to suggest that the committee consider the one being proposed and advanced by Senators Grassley, Levin, Boren, and Schmitt as an amendment to S. 1080, the regulatory reform bill.

It reduces the holding period for congressional review substantially, and it speeds up the floor debate on the resolution of disapproval. We also believe it should be added with a specific nonseverability clause so it is completely clear what the conditions for the delegation of authority to the FTC are.

And if I might just, one quick final word on another topic of these hearings, the NFIB was pleased to note the recent statements by the chairman and Senator Packwood that the antitrust enforcement role of the FTC was not to be one of the areas that the committee was going to tamper with. The NFIB believes that the antitrust role of the FTC should remain intact and not be restricted in any manner.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF MICHAEL ROUSH, LEGISLATIVE REPRESENTATIVE, NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Mr. Chairman: It is a pleasure to be here today in order to present the views of the National Federation of Independent Business (NFIB) and its 500,000 small business owner-members on the issue of "the authority of Congress to veto newly-issued agency rules."

Oversight and control of the regulatory process is long overdue. NFIB has, for several years, regularly surveyed the problems of small business. The top four concerns consistently cited by small business, since the inception of our survey in 1974, have been inflation, taxation, the cost of money, and government regulation. We regard these issues as stemming from the same basic source, the increasing influence that the government has over private economic decisions. The incredible level of involvement of the government in the credit markets, due to a rapidly expanding federal budget, has shrunk the availability of credit to small business and resulted in erratic and intolerable interest rates. It will be difficult to remedy these problems, but NFIB is confident that the necessary program of spending cuts will be quickly enacted.

Regulation is directly relevant to these concerns. It is a serious problem for our economy and for small business in particular. The imposition of regulatory requirements have affected the decisions of business owners in direct money terms and in less calculable ways. Compliance costs of new equipment, or procedures, recordkeeping and reporting and the professional assistance necessary to interpret and comply with the regulatory requirements are a direct government imposed "tax" on the business owner.

In the words of the first Annual Report on Small Business and Competition submitted by President Reagan to Congress, March 1982: "During the 1960's and 1970's a large number of Federal regulatory agencies were established. The resultant regulatory activity, which is in many instances uncoordinated, unintegrated and sometimes unnecessary, causes a heavy and accumulating cost burden on small business. A 1979 SBA study revealed that paperwork burdens alone cost small business $12.7 billion per year. A research study funded by the SBA and conducted by Battelle Human Affairs Research Center demonstrated that regulatory costs are exponentially higher per unit of sale for firms with fewer than 50 employees than for larger firms."

But, perhaps of even greater importance are the indirect results of much of government regulatory activity. It is impossible to gauge how many times a small business found itself unable to enter a market, develop a new product or provide a competing service because the costs of regulatory compliance have created an entry barrier. The President's Annual Report on Small Business and Competition states that "There is considerable evidence that uniform application of regulatory requirements increases the minimum size of firms that can compete effectively in the regulated market." Thus regulatory activity of the government has done much to reinforce the static structure of American industry, by deterring the growth and productivity of small business. It is essential for small business that this regulatory structure which has grown so rapidly in the past two decades be rationalized and pruned.

There have been innumerable speeches made by public figures of all manner of political persuasion about the evils of regulations and the need to do something about it. The Regulatory Reform Act, S. 1080, is a positive result of that concern. *Yet without legislative review and possible veto of regulations, regulatory reform will be incomplete from small businesses' point of view.* NFIB regards legislative veto proposals like the one currently in the FTC's authorizing legislation to be among the simplest and most direct methods of introducing an accountability to the federal regulatory structure. We believe that legislative veto, in conjunction with other efforts currently being made by the Congress and the Administration, will correct regulatory excesses, and occasion the careful scrutinizing of the regulatory process which has been lacking for so many years. NFIB, therefore, strongly supports the inclusion of a legislative veto provision in this year's FTC reauthorization bill and urges this Committee to report such a bill to the full Senate.

Neither NFIB nor any other responsible spokesman can make a case that regulation is never appropriate. There are some issues which may require a level of government involvement in order to assist the workings of the marketplace. By the same token, every time the government does attempt to get involved in regulating the conduct of citizens or institutions, it must carry the burden of proving that the regulation proposed is fully justified.

Congress has necessarily established a fairly loose statutory framework in a number of areas. The details of a certain issue can rarely be absolutely anticipated by the Congress when it authorizes a general regulatory statute or a series of regulatory policies or programs. The specifics of a problem, of an industry, of current conditions are most often left to the agencies, such as the FTC, to address with their discretionary authority. But, as has been carefully argued in testimony before numerous Congressional Committees over the years, the administrative discretion of regulatory agencies is directly linked to the legislative authority of the Congress. In fact, NFIB believes that substantive rulemaking by administrative agencies is a delegated legislative function that remains part of the legislative process and is subject to such procedural requirements, limitations, and conditions as Congress sees fit to impose in order to preserve the integrity of that process as well as to fulfill its constitutional responsiblity as the ultimate federal lawmaker.

When the Congress grants to an agency a broad discretionary mandate, this inevitably raises the question of how to ensure the accountability of an agency to its statutory mandate. Obviously, the primary responsibility of the Congress is to look to the authorizing statute to ensure that it is clear and responsive to changing conditions. The best way to see that an agency is performing as the Congress intended is to regularly review the statutes and authorized programs. The underlying statutes should be modified if programs and regulations are unnecessary or improper. This is admittedly not an easy task. But a clear and updated statement of Congressional intent in an authorizing statute will be an obvious signal to an agency of its proper direction. For instance, a few years ago much criticism was being leveled at the Interstate Commerce Commission for regulatory actions it was taking on motor carrier issues. The 96th Congress passed the Motor Carrier Act of 1980, the first comprehensive review of this area of regulation in 45 years. This legislation now is available as a much clearer and more relevant benchmark for the ICC to refer to in discharging its regulatory duties.

Likewise the reconsideration of sections of the Clear Air Act may occur in this Congress. A possible rewrite of the telecommunication laws will dramatically affect the powers and responsibilities of the FCC. These debates over the substance of regulation are the primary battlegrounds of regulatory reform. No amount of tinkering with the process of regulation will substitute for the reasoned and current statements of Congressional intent which must be available to guide agency discretion.

There are, of course, many situations in which a relevant or precise statutory standard is not available to guide an agency or is available but is not followed by the agency. In those cases some checks on the regulatory process or the results are necessary. The Senate debate on S. 1080 will revolve around various proposals to require certain regulatory analysis during the regulation writing process. The last Congress enacted a precedential law, the Regulatory Flexibility Act, which requires all agencies to articulate, at the time a regulation is issued, important information about the costs and reasons for the regulation, and why the agencies made that particular regulatory choice. However, all these proposals and statutes focus on the formal process of rulemaking and cannot guarantee any particular result. Hopefully, the regulatory result will be reasoned and clearly justified. Legislative review and veto of regulations would focus on the policy implications of the result of the regulatory process. It would enable the Congress to render a direct judgment on whether the agency exceeded its statutory bounds in a particular regulation. Establishment of a legislative veto mechanism would be a significant shift in the real power of government away from the bureaucracy and back to the elected Congress. It would make it clear that, insofar as public policy and lawmaking are concerned, the agencies are the agents and creatures of Congress, not its masters, or even its equals.

NFIB is aware of the Constitutional questions that have been raised against the concept of legislative veto, but until the Supreme Court addresses the issue it is entirely appropriate, is indeed necessary, for Congress to proceed in the exercise of what it views as its Constitutional legislative mandate. The case immediately before the Court touching on this issue is not a sufficient generality to warrant delay by this Committee, or the Congress, on reauthorizing the FTC *with* a legislative veto as part of it. The vast majority of NFIB's members believe that the legislative veto is a thoroughly Constitutional exercise of the Congress's powers and urge rapid adoption of a legislative veto not only for the FTC but for all federal rulemaking agencies, executive and independent alike.

Mr. Chairman, the support for the legislative veto idea that I have expressed today is widespread in the public at large and, particularly, in the small business community. As evidence: NFIB's entire 500,000 members were polled on this issue, 76 percent favored it, 21 percent opposed it, and 3 percent were undecided; legislative veto was the number five recommendation of the 1980 White House Conference on Small Business (enclosed); legislative veto was recommended by a 30 association task force on small business issues as recently as January, 1982 (enclosed); the Congress passed and the President signed H.R. 3982, last year's Reconciliation bill which contained nine legislative veto provisions; and, the Southern Lumber Manufacturers Association, the American Farm Bureau Federation, the National Association of Realtors, the National Association of Home Building, the Associated Builders and Contractors, and the Independent Petroleum Association of America among others are currently supporting the adoption of a legislative veto provision for all government agencies as part of the Regulatory Reform Act.

The small business community commends this Committee for focusing on the legislative veto concept as part of its FTC reauthorization hearings and hopes that it will report a reauthorization bill to the full Senate with legislative veto as part of it.

A final, quick word on one other aspect of these hearings. NFIB has noted with pleasure that both Senator Kasten and Chairman Packwood have indicated that they do not intend to change the anti-trust authority vested in the FTC. Our members view with alarm proposals to reduce or eliminate the FTC's long standing role in anti-trust enforcement and, therefore, support your resolve not to weaken one of the two legs of our nation's anti-trust enforcement effort.

Thank you very much.

Senator KASTEN. Next we have Prof. Eugene Gressman from the University of North Carolina, School of Law.

Mr. GRESSMAN. Thank you, Mr. Chairman. I would like my written statement to be made part of the record.

Senator KASTEN. Without objection, so ordered.

Mr. GRESSMAN. And I would, therefore, just give you a brief summary of my position which is that the legislative veto provision which was written into the Federal Trade Commission Act in the amendments of 1980 is totally and completely constitutional.

As you may know, I have served as special counsel to the House of Representatives in defending the constitutionality of this device in virtually every piece of litigation where the matter has been raised, along with and in opposition to my friend at the other end of the table, Mr. Morrison. We have just finished arguing the veto provision as it appears in the Immigration and Nationality Act before the Supreme Court. And I am sure we will meet again in the Supreme Court chambers next term to be arguing the constitutionality of the veto provision respecting Federal Energy Regulatory Commission regulations, which was recently held unconstitutional by the court of appeals for the District of Columbia.

Basically, as I view this device, it is a procedure whereby Congress has deemed it appropriate and necessary and proper as an implementation of Congress power, in this instance over interstate commerce. In short, it reflects a choice of means; a choice confided in Congress by virtue of the affirmative legislative authority given by the necessary and proper clause of article I, section 8.

The critical feature of this choice of means that emerges from this device, as it is written in the Federal Trade Commission Act, is that it constitutes a limited delegation of quasi-legislative power to the administrative agency, the Federal Trade Commission. A delegation, in other words, of the quasi-legislative function of administrative lawmaking.

The device which permits congressional review and possible disapproval reflects the fact that the delegation to the Federal Trade Commission is limited to proposing or recommending legislative type rules and regulations before they have become effective as a matter of law. Congress has simply retained its legislative prerogative to determine when and if a proposed regulation should become finally effective.

The commission, in other words, has not been delegated authority to finally promulgate a proposed regulation, and the agency, in accordance with well-established Supreme Court precedent, must respect the limitations placed upon it by Congress in the delegation.

One final thought is important to remember in this connection, and that is that in this kind of delegation of quasi-legislative functions to the administrative agency, the agency itself is not performing any executive or judicial function. It is performing what the Supreme Court has said time and again, a quasi-legislative function delegated to it by the Congress.

Now, I suggest that a proper understanding of what this legislative veto device means and how it operates compels the conclusion that the choice of that kind of means of exercising the legislative authority of the Congress is consistent with all other provisions of the Constitution, and it is certainly not prohibited by any other provisions of the Constitution.

The executive seeks to outlaw the use of this device on two grounds. One is the general separation of powers doctrine. I suggest that the doctrine has no application here, because, as I have already mentioned, this device in no way implicates the use of executive or judicial powers by the administrative agency. And so far as the presentation clause is concerned in article I, section 7, it is simply not directed at this kind of delegation of quasi-legislative authority to administrative agencies. That is not lawmaking in the sense in which article I, section 7 pertains.

[The statement follows:]

STATEMENT OF EUGENE GRESSMAN [1]

This statement is devoted to the proposition that the device commonly known as the "legislative veto" is constitutional. I have particular reference to the kind of "legislative veto" contained in Section 21(a)(1) and (2) of the Federal Trade Commission Improvements Act of 1980, 94 Stat. 393, 15 U.S.C. § 57a-1(a)(1) and (2), i.e., a two-House "legislative vote" procedure whereby proposed "final rules" may be disapproved by concurrent resolution of both Houses before such proposed rules become legally effective.

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1. *The basic statutory scheme of a "legislative veto."*—Essential to understanding the constitutional implications of the so-called "legislative veto" is an appreciation of the basic statutory scheme in which this legislative device appears. There appear to be two characteristics in every scheme wherein Congress seeks to review and approve/disapprove rules and regulations submitted to it by an administrative or executive agency:

(a) The statutory scheme in every instance reflects a delegation by Congress of a limited or conditioned quasi-legislative power, the terms and conditions of the delegation being set forth in a duly enacted statute. Such statutes make clear that the delegation to the administrative agency does not include the legislative function of determining whether or when the administrative rule or regulation shall become effective so as to have the force of law.

(b) Under the typical statutory scheme, the agency (such as the FTC) is delegated the quasi-legislative but limited function of merely proposing or recommending to Congress those rules which the agency believes Congress should approve and make effective as rules of law. In this connection it is generally wise to refer in the statute to the rules being recommended by the agency to Congress as "proposed" or "recommended" final rules.

If those statutory characteristics are clear, the ensuing constitutional justification for the "legislative veto" device becomes quickly evident. And once those characteristics are evident, the statutory procedure whereby one or both Houses may disapprove a recommended rule or regulation cannot be described as a legislative "veto." Congress is not "vetoing" an established, final rule of law promulgated by the agency. It is merely refusing to allow a recommended rule to become effective, just as either House can refuse to allow a bill proposed by a Senator or Representative to become effective as a law.

2. *The basic constitutional analysis.*—The basic analytical tool for assessing the constitutionality of Acts of Congress was established long ago by Chief Justice Marshall in *McCulloch* v. *Maryland*, 4 Wheat. (17 U.S.) 316 (1819). The Supreme Court has utilized the *McCulloch* model literally hundreds of times in testing the validity of congressional legislation. And the Court of Claims faithfully followed the *McCulloch* model in validating the so-called "one-House veto" provision in the federal Salary Act. *Atkins* v. *United States*, 556 F.2d 1028 (Ct.Cls. 1977), *cert. denied*, 434 U.S. 1009 (1978).

The *McCulloch* test focuses upon the great sweeping clause of Article I, Section 8, Clause 18—the Necessary and Proper Clause. The Constitution there vests in the Congress the affirmative power to make all laws "which shall be necessary and proper for carrying into Execution [1] the foregoing Powers [vested by Section 8 in the Congress], and [2] all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof." The great bulk of congressional legislation stems from the exercise of this vast "necessary and proper" power. Under part [1] of the Clause, Congress is enabled to legislate so as to implement the 17 substantive powers vested in it by the "foregoing" clauses of Section 8—known as the "vertical" thrust of the Clause. And under part [II] of the Clause—known as the "horizontal" thrust—Congress can and does enact laws to enable the Executive and the Judiciary to perform their respective functions. It is through the "horizontal" thrust of the Clause that Congress is authorized to enact legislation that delegates quasi-legislative functions to executive and administrative agencies, thereby implementing their proper functions.

Chief Justice Marshall was the first to articulate the critical role that the Necessary and Proper Clause plays in the enactment of legislation. And his opinion in *McCulloch* laid down the famous three-part test for assessing the validity of statutes stemming from an exercise of the legislative power conferred by that Clause.

Chief Justice Marshall stated the three-part *McCulloch* test as follows:

(a) *"Let the end be legitimate, let it be within the scope of the constitution* * * * " 4 Wheat. at 421. In other words, one first looks to the legislative, executive or judicial power being implemented by the "necessary and proper" legislation to see if that power, or end, is vested by the Constitution in the relevant branch of Government.

(b) " * * * *and all means which are appropriate, which are plainly adapted to that end* * * * *are constitutional.*" 4 Wheat. at 421. In other words, one next looks to the means, the "necessary and proper" means, that Congress deems appropriate to implement a legitimate end. As *McCulloch* determined, what Congress deems appropriate is usually decisive, not being subject to judicial second-guessing.

(c) Finally, of course, the means which Congress deems "appropriate" must "*not [be] prohibited, but consistent with the letter and spirit of the constitution* * * * ." 4

Wheat. at 421. In other words, the Necessary and Proper Clause does not permit Congress to make laws that are proscribed by some other provision of the Constitution, such as the Due Process Clause of the Fifth Amendment. The "means" selected must be consistent with all other provisions. But *McCulloch* added that before the words of some other provision may be said to impede or proscribe the congressional choice of "means," those other words must "imperiously require" a restriction on the choice of means. 4 Wheat. at 408.

3. *Application of the McCulloch test to the concurrent resolution version of the "legislative veto" device.*—The constitutionality of the legislative review procedures contained in the 1980 amendments to the Federal Trade Commisson Act is clear upon application of the *McCulloch* test.

(a) Without question, the whole of the Federal Trade Commission Act—including the legislative review procedures in the 1980 amendments—is directed to the "legitimate end" of executing the vested power of Congress over interstate commerce.

(b) The "means" Congress has deemed "appropriate" to the execution of its power over interstate commerce is, of course, the Federal Trade Commisson Act, as amended, including the legislative review procedures embodied therein. More particularly, Congress has deemed it "appropriate" to delegate to the FTC certain limited quasi-legislative functions with respect to formulating interstitial rules of law. Congress has simply declined to give the FTC full and final authority to promulgate the "substantive rules" or "legislative-type rules" necessary to fulfill the legislative purposes of the Federal Trade Commisson Act.

The Supreme Court has repeatedly recognized that administrative agencies can exercise such quasi-legislative power to promulgate these "legislative-type rules," within the ambit of a given statute, only at the sufferance of Congress. As the Court said in *Chrysler Corp.* v. *Brown*, 441 U.S. 281, 302 (1979), "The legislative power of the United States is vested in the Congress, and the exercise of quasi-legislative authority by governmental departments and agencies must be rooted in a grant of such power by the Congress and *subject to limitations which that body imposes.*" [Emphasis added]. And so when Congress limits the power of the FTC to issue these substantive rules, the FTC is bound to respect those limits. In other words, the FTC lacks any vested constitutional power to formulate those rules other than in conformity with the limits and conditions imposed by Congress.

In sum, Congress has deemed it "appropriate," in execution of its legislative powers under the Necessary and Proper Clause, to limit its delegation of quasi-legislative powers to the FTC. The FTC can only propose or recommend to Congress the "legislative-type rules" it thinks Congress should approve and finalize. *McCulloch* makes clear that such an "appropriate" delegation is constitutional.

(c) Such an exercise of legislative power under the Necessary and Proper Clause does not appear prohibited by or inconsistent with "the letter and spirit of the constitution." None of the constitutional provisions relied upon by the Executive can be said to "imperiously require" that Congress be forbidden from selecting this particular "means," this kind of limited delegation of quasi-legislative powers.

Certainly the Executive's reliance on the general separation of powers doctrine is misplaced. The legislative decision to delegate certain limited quasi-legislative functions to the FTC in no way implicates the executive powers vested by Article II or the judicial powers vested by Article III. When the FTC proposes or recommends "legislative-type rules" it is performing what the Supreme Court calls quasi-legislative functions. And when Congress reviews and either approves or disapproves such recommended rules, it is performing a pure legislative function. Neither the Executive nor the Judiciary have any function to perform with respect to the promulgation of such rules other than in accordance with specific statutory authorization.

Nor does the Executive's reliance on the Presentation Clauses of Article I, Section 7, stand on any surer footing. Those Clauses generally require that every bill that has passed both Houses, and every "Order, Resolution, or Vote to which the Concurrence of the Senate and House of Representatives may be necessary," shall be presented to the President for approval or disapproval. Such is the bicameral process for enacting new legislation.

But neither the letter nor the spirit of those Clauses even begin to address the problem of adopting "legislative-type rules" within the bounds of a duly enacted statute. The whole area of administrative law-making, which stems from congressional delegation by statute of quasi-legislative functions, simply escapes the reach or the concerns of the Presentation Clauses. Administrative law-making can best be described as mini-legislation that never rises to the level of the bicameral and presentation requirements of Article I, Section 7. It is mini-legislation that is designed to fill in the interstices of a statute enacted in accordance with Article I, Section 7.

How Congress deals with such mini-legislation has been left to its discretionary legislation powers under the Necessary and Proper Clause.

Indeed, were the Presentation Clauses to be applied to the administrative lawmaking processes, utter chaos would ensue. If congressional review and approval/disapproval of proposed "legislative-type rules" really involves some change in established law so as to require that the change be subjected to the full bicameral process, then how does eliminating such congressional review and thereby delegating to the administrative agency full and final power to effectuate such rules become anything less then unconstitutional law-making by the agency? Why is an administrative agency any less subject to the Presentation Clauses than Congress itself, if we assume that this type of quasi-legislative functioning involves the enactment of new law?

The ultimate answer seems inescapable. When Congress is dealing with this kind of mini-legislation, the Presentation Clauses do not apply. Rather, the Necessary and Proper Clause gives Congress a high degree of flexibility in determining the procedures for processing administrative rule-making. Congress can do the job itself, in whole or in part, or it can delegate some or all of the function to an administrative or executive agency. That freedom of choice is what the Necessary and Proper Clause is all about.

It should be noted that the procedures adopted in the 1980 amendments to the Federal Trade Commission Act involve the use of the concurrent resolution device for expressing congressional disapproval of proposed FTC rules. As Section 396 of the current Jefferson's Manual of Parliamentary Procedure notes, in modern practice a concurrent resolution is not legislative in nature and thus need not be sent to the President for approval.

Legislative review of proposed administrative law-making is indeed constitutional. There is nothing in the Constitution that imperiously prohibits it.

Senator EXON. Mr. Chairman, could I ask one quick question? I really have to leave.

Senator KASTEN. Surely, Senator Exon.

Senator EXON. Professor Gressman, if your interpretation of the constitutionality, then, is correct, then my question is, does it presume that you would have to have a two-House veto, or would a one-House veto suffice? My point being in all the laws we make here, they are passed by two bodies. It would seem logical then, to substantiate the position that you are advancing, you would have to have a two-House veto; you could not do it with a one-House. Is that a fair assumption of your position?

Mr. GRESSMAN. I do not think that necessarily follows. I think many of the veto provisions, as you know, are of the one-House variety. And I have argued and defended both types. In fact, I understand there are as many as seven different varieties of legislative veto. Some include a 1½-House veto.

But no, the point is that I think that when this body is sitting to review a proposed regulation, I think one House or two Houses, as Congress sees fit, certainly have the authority to reject a proposal.

Senator EXON. And I assume, therefore, that if the Senate passed a law and later, if the Senate said that is the wrong interpretation, then in essence what you are saying is since the Senate was at least half of the thrust toward passing the legislation and therefore it would not have passed without that understanding of the Senate, that you could have a Senate veto only. Is that correct?

Mr. GRESSMAN. That is I think essentially correct. It is simply—the analogy is that any Senator or Representative can make a proposal. Now, the refusal of one House to accept the Member's proposed bill is similar to what we are dealing with here. I suppose you could say there that one House is vetoing the proposed bill.

Senator EXON. But one House could veto it in the original instance by not passing it.

Mr. GRESSMAN. That is right.

Senator EXON. Thank you, I appreciate that.

Senator KASTEN. Mr. Alan Morrison, director, Public Citizen Litigation Group. Mr. Morrison.

Mr. MORRISON. Thank you, Mr. Chairman. Let me begin by saying that my association with the constitutionality of the one-House veto is, like Mr. Gressman's, not neutral. I have represented Mr. Chadha in the case decided by in the ninth circuit and now argued before the Supreme Court, and I represented the consumer groups that won the recent victory in the D.C. Circuit, both of which declared the one-House veto unconstitutional.

It is my view that in all likelihood, the Supreme Court will rule in the *Chadha* case by June of this year and we will have a better idea on the constitutional question. In addition, the *Consumer Energy Council* case is going to the Supreme Court, and I expect that the Supreme Court will decide by June whether it will take it and in what form and so forth, and set it down for argument next year if it decides to take it. That is the simple, the easy part.

Second, my position is also easy, and that is, I believe that all vetoes—two Houses, one House, any size, shape or form—are all unconstitutional. Rather than go into it at great length, I have a copy of my brief that I filed in the Supreme Court, and I would like to make it available for the committee for consideration by the members of the staff, rather than try to summarize it here in no more than just in a sentence or two.

I would also say, Mr. Chairman, that if the position taken by the defenders of the veto, including Mr. Gressman here today, is accepted, the logic of their position is that because Congress can place a condition upon a rule going into effect, it can place almost any condition and therefore, we would not require two Houses or one House. Then a committee, a subcommittee, or a single designated individual could, if this position is sustained, manage to veto a regulation. There is, constitutionally speaking, no stopping point.

Third, the position taken in defense of the veto is that we really do not have a veto at all. What we have is a proposed regulation or a recommendation which comes forth to the Congress, and if the Congress does not disapprove it, that is if one House or other does not disapprove it or two Houses do not disapprove it, then it goes into effect.

The difficulty is that our constitutional system simply does not provide for recommendations going into effect by silence or, as you said in your opening statement regarding the technical amendment to one of the FTC rules, by the passage of time.

The Constitution provides the means by which legislation is enacted: two Houses plus a concurrence of the President. It is my position, and it is also the position of the executive branch in the *Chadha* case and elsewhere, that unless you have the complete process by which legislation is enacted, have that repeated in connection with rules, then the process is invalid the veto must be set aside.

Now, I do want to make it clear, however, that this does not apply to the so-called wait and see provisions or the lay and wait provision under which Congress says that no rule may go into effect for a period of 60 days, and if during that time Congress passes a statute or a joint resolution. They are not the same because they both require Presidential approval, then the rule shall not go into effect. That is perfectly legitimate because it requires the constitutional means for legislation. But anything short of that is unconstitutional.

Finally, let me just say a word—I am sorry that Senator Exon had to leave, because he raised a question about what happened if the Senate disagreed with the interpretation of a statute and for that reason vetoed an agency rule, would that be proper. The answer in our view is it would not be constitutional because at that point the Senate would not be performing a legislative function but a judicial function. And in our system of separation of powers, that is a job that is assigned to the Judiciary and cannot be undertaken by the Congress, either House or both Houses acting together, unless the President concurs.

That concludes my statement, thank you.

Senator KASTEN. Mr. Jay Angoff, Congress Watch.

Mr. ANGOFF. Mr. Chairman, I am Jay Angoff. I am a lawyer with Congress Watch and I very much appreciate the opportunity you have given me to testify here today.

I would like to talk now not about the constitutionality of the legislative veto, but rather, how the veto legislative veto of FTC rules has worked in practice. We really have had one opportunity to see how the legislative veto is working or rather is not working; that was with the attempt of Congress to veto the FTC used car rule. And frankly, this attempt by Congress to kill the FTC used car rule confirms the worst fears of opponents of the legislative veto.

As you know, in 1975, in the Magnuson-Moss Act, Congress directed the FTC to come up with a rule having to do with used cars. After a 6-year investigation, 950,000 page record, hearings all across the country, the Commission staff came up with a rule that would require used car dealers to inspect their cars. The five commissioners said that rule was too strong; it imposed too great a burden on business. They sent it back down to the staff. The staff came out with a weaker rule, the Commission said that rule is still too strong, it still imposes too great a burden on business.

So finally, in August of this year the Commission came up with the weakest rule one could ever imagine that is simply a rule that requires used car dealers to tell the truth to consumers. And that is if they know brakes on the car do not work they have to tell the consumer that the brakes do not work.

Now, who could be opposed to this rule? Well, in September, the National Auto Dealers Association had their annual convention in Washington. They decided to oppose the rule, and a few days after that, almost 100 members of Congress cosponsored the bill to kill the rule.

Moreover, before this committee or the House Commerce Committee could even have hearings on the rule—that is, on the resolution to kill the rule—almost one-half the members of both Houses had cosponsored bills to kill it. Now, who benefits from this process? Consumers clearly do not benefit, the FTC clearly does not benefit. But more important for these purposes, Congress does not benefit. Congress has much more important things to do with its time than to argue about the FTC's used car rule.

More important, when the public sees a spectacle like the Congress trying to kill a simple rule requiring used car dealers to tell the truth, it undermines the faith of the public in Congress and in the integrity of the legislative process.

Now, it is no secret that the National Auto Dealers Association's Political Action Committee gave more than one-half million dollars to the Members of Congress who cosponsored the bills to kill the rule. Some Members of Congress came right out and say yes, votes are traded for money. Former Congressman Vanick said that. The other day on national TV two very moderate congressmen, Mike Synar and Jim Leach said that, but we do not go that far, you do not have to go that far. But it seems to be a little naive to think that all this money just has no effect.

Now, that is not to say that campaign contributions cannot have an effect without a legislative veto. For example, today we see that the AMA, the American Dental Association, and the America Optometric Association have given almost $1 million to the Members of Congress who have cosponsored the bill that they want. That is, of course, the bill to exempt the professions from the Federal Trade Commission Act.

So clearly, campaign contributions can have an influence without the legislative veto. But we think that the legislative veto is tailor made; it is simply an invitation to special interests who have been unable to make their case on the basis of the facts and the law before an impartial adjudicator to come to Congress and make their case on the basis of heavy lobbying and heavier campaign contributions.

Now in conclusion, the most disillusioning thing about what this committee is trying to do to the FTC right now is to see the absolutely overwhelming influence of business on the political process. One expects business to overwhelm labor or consumers. One takes that for granted. But one does not expect business to overwhelm Congress.

In law school you learned the Clayton-Sherman, one of the first antitrust laws, Senator Kefauver wanted the amendments to the Sherman Antitrust Act, but today nobody asks what does Senator Cannon want, what does Senator Ford want. Rather, they say what does the Chamber want and what does NAM want and what do the dentists want and what does the AMA want.

On behalf of these people who are not dentists or members of the AMA or members of the Chamber or NAM, I would like to ask this committee to look back at what Congress said in 1914 when it enacted the FTC Act, when it created the FTC as an independent agency immune from political influence, and to allow the FTC to do its job and to get business influence out of what Congress intended to be an impartial decisionmaking process.

Thank you.

[The statement follows:]

STATEMENT OF JAY ANGOFF, STAFF ATTORNEY, PUBLIC CITIZEN'S CONGRESS WATCH

Mr. Chairman, Members of the Committee: My name is Jay Angoff and I am a Staff Attorney at Public Citizen's Congress Watch, a public interest advocacy group founded by Ralph Nader. Public Citizen is a nationwide consumer organization with approximately 70,000 contributors annually.

We applaud the firm stand you have taken in favor of retaining the FTC's traditional role in antitrust enforcement. As you have recognized, a strong FTC enforcement arm is vital to ensuring that our free market system can function without being restrained by monopolistic and anticompetitive practices.

Equally important to the functioning of the free market system, however, is the Commission's ability to prevent unfair or deceptive acts or practices. We are seriously disturbed by reports that certain groups are seeking, under guise of "clarification," to both weaken the FTC's authority to prohibit unfair or deceptive acts or practices and to carve out special exemptions from the laws the rest of us must obey for certain upper-income "professionals." We are particularly disturbed at reports that this Committee is taking as its starting point the proposition that the FTC's authority to protect consumers must be cut back and that the only relevant question is the extent to which that authority is to be restricted.

We respectfully suggest that the FTC's authority to root out unfair or deceptive acts or practices is just as important to the unfettered functioning of the free market as are its antitrust enforcement powers. It should be retained and strengthened, not weakened or "clarified."

Nevertheless, business clearly does want to weaken the FTC. Our views on the issues various business groups want this Committee to consider are set forth below.

I. THE FTC'S "UNFAIRNESS" JURISDICTION

When Congress enacted the FTC Act in 1914, and the Wheeler Lea amendments to the Act in 1938, it deliberately did not define the term "unfair" because it wanted the concept of unfairness to grow and develop as times and circumstances changed. What Congress emphasized in 1914 in enacting the FTC Act is perhaps even more true today: "It is impossible to frame definitions which embrace all unfair practices. There is no limit to human inventiveness in this field * * * Whether competition is unfair or not generally depends upon the surrounding circumstances of the particular case. What is harmful under certain circumstances may be beneficial under different circumstances."—H.R. Conf. Rep. No. 1142, 63rd Cong., 2d Sess., at 19 (1914)

The Supreme Court has recognized and approved the wisdom of this approach. As the Court emphasized in *FTC* v. *F.R. Keppel & Bro.*, 291 U.S. 304, 310, 312 (1934), "Neither the language nor the history of the act suggest that Congress intended to confine the forbidden methods to fixed and unyielding categories . . . Congress, in defining the powers of the Commission, thus advisedly adopted a phrase which, as this Court has said, does not admit of precise definition, but the meaning and application of which must be arrived at by what the court elsewhere has called 'the gradual process of judicial inclusion and exclusion.'" [citations omitted]

Judge Learned Hand has stated that the Commission's duty under its "unfairness" jurisdiction "is to discover and make explicit those unexpressed standards of fair dealing which the conscience of the community may progressively develop." *FTC* v. *Standard Educ. Soc'y*, 86 F.2d 692, 696 (2nd Cir. 1936), *rev'd on other grounds*, 302 U.S. 112 (1937). Or in the Commission's own words, "* * * unfairness is potentially a dynamic, analytical tool capable of progressive, evolving application which can keep pace with a rapidly changing economy. Thus as consumer products and marketing practices change in number, complexity, variety and function, standards of fairness to the consumer may also change." *Pfizer*, 81 FTC 23, at 61 (1972).

The Commission has carefully set out its standards for determining whether a specific act or practice is unfair in its December 17, 1980 policy statement. By issuing this policy statement, the Commission has done the lawyer's work for him, by distilling the results of judicial and legislative history into one succinct document.

To enact that document into law, however, would be to set in stone a concept that Congress meant to be flexible—to do what for almost 70 years Congress and the courts have said should not be done. As University of Wisconsin law professor Gerald Thain told this subcommittee in April, 1980, "[A]lteration of the unfairness standard would emasculate the FTC's power to treat continually evolving, new forms of improper commercial behavior. To the extent that the unfairness doctrine is dismantled, the consuming public will lose one of its most important protections against the unscrupulous and harmful conduct of that small group of businesses willing to engage in such conduct."

We therefore urge this Committee to stand firm against any efforts to restrict the ability of the FTC to protect the free market against unfair acts or practices, and to allow the concept of unfairness to remain flexible, as Congress and the Courts originally intended.

II. DECEPTION

The FTC's jurisdiction over "deceptive" acts or practices has not been controversial. As common sense would indicate, prohibiting deceptive practices is to the advantage of both the consumer and the vast majority of businesses—both large and small—that do not deceive their customers.

Nevertheless, reports have surfaced of various groups trying to cut back—again under the guise of "clarification"—the ability of the Commission to prohibit "deceptive" acts or practices. We believe any such effort is totally indefensible, and that the vast majority of businesspeople, who do not deceive consumers, would also view any such effort as indefensible.

We therefore urge this Committee to oppose any efforts to undermine the ability of the FTC to prohibit deceptive acts or practices.

III. SECTION 5(m)(1)(B)

In the Magnuson-Moss Act of 1975, Congress included a provision that would enable the Commission to more effectively police the free market against unfair or deceptive acts or practices and at the same time save the FTC—and the American taxpayer—a substantial amount of money. Under what is now § 5(m)(1)(B) of the FTC Act, the Commission may fine any person engaging in a practice it has found unlawful up to $10,000 per violation. Prior to Magnuson-Moss, any company could engage with impunity in practices the FTC had found unlawful except for the original company the Commission had proceeded against. The only way the FTC could stop a company not the subject of its original action from engaging in practices it had already found unlawful was to start all over again and try the same case against that company that it had already tried against the first company.

The FTC's congressionally-mandated power under section 5(m)(1)(B) has proved to be one of the most effective and efficient law-enforcement tools the Commission has. Since Congress gave the FTC this authority in 1975, it has brought 31 cases and obtained $1,000,000 in civil penalties against firms that had knowingly engaged in a practice the FTC had declared illegal. To have proceeded separately against each firm would undoubtedly have cost the Commission—and generated legal fees—many times the amount obtained by the Commission in civil penalties.

We therefore urge this Committee to resist any pleas to undermine the Comission's section 5(m)(1)(B) authority.

IV. EXEMPTIONS FROM THE ANTITRUST AND CONSUMER PROTECTION LAWS FOR CERTAIN INDUSTRIES AND PROFESSIONS

A. Special exemptions for lawyers, doctors, dentists and other high-income "professionals"

Bills have been introduced in both houses that would exempt certain upper-income "professionals" from the laws the rest of us must abide by. If any such bill were passed, doctors and lawyers could engage in unfair or deceptive acts or practices with complete immunity from FTC attack, while small businessmen or anyone else not a "professional" who attempted to engage in such practices would remain fully subject to FTC scrutiny. To require ordinary people to obey the law while exempting upper-income "professionals" from obeying the law is patently unfair.

Moreover, it has been in the area of "occupational deregulation"—the elimination of both private and governmental regulations which both raise prices to consumers and restrict output—in which the FTC has had its greatest successes and from which consumers have received the most direct and substantial benefits. For example, after the Commission held that restrictions on advertising the price of contact lenses were unlawful, contact lens prices dropped dramatically, saving consumers more than $100 million annually, according to the FTC. The FTC has also challenged restrictions on advertising, boycotts and conspiracies by doctors and dentists. Its decision challenging the American Medical Assoication's prohibitions on truthful advertising and prepaid medical services is currently pending before the Supreme Court.

We respectfully suggest that attempts by so-called "professionals" to exempt themselves from the laws the rest of us must obey are the most blatant kind of special-interst pleas and should be rejected out of hand.

B. Priviliged treatment for certain industries enacted in 1980

During the unfortunate assault on the FTC of 1979-80, Congres exempted certain industries from FTC jurisdiction and prohibited the FTC from continuing proceedings involving certain industries or companies. Clearly, what has come to be known as "the rape of the FTC" was not one of Congress's finest hours. We respectfully suggest that any exemptions for certain industries be brought to an end in this year's FTC authorization bill.

V. LEGISLATIVE VETO

Another unfortunate provision that found its way into the 1980 FTC Act amendments was the one allowing Congress to kill any FTC rule—for any reason or for no reason—before it could take effect.

Judicial and popular response to the legislative veto has not been favorable. In 1980, the Court of Appeals for the Ninth Circuit handed down a decision holding a legislative veto provision unconstitutional. The Supreme Court is likely to decide the appeal of that case in June. On January 29 of this year, the Court of Appeals for the D.C. Circuit held the FERC legislative veto provision unconstitutional. Noting that "legislative veto authority allows special interests to achieve their ends by pressuring administrative agencies through congressional committees," the court unanimously held that Congress infringes on the power of both the executive and judicial branches of government when it vetoes agency rules.

In addition, the first test of the FTC legislative veto—the FTC's used car rule—has confirmed the worst fears of opponents of legislative veto. The used car rule, which had been promulgated after a six-year, 50,000-page investigation and hearings throughout America, would merely require used car dealers to disclose tro consumers any defects they know about in their cars and any guarantees they offer. It had been weakened twice, under congressional and used-car dealer pressure, from the FTC's original proposal. Nevertheless, even before congressional hearings had been held on the rule, almost half the U.S. Congress had co-sponsored resolutions to kill it. Understandably, this rush to kill a rule merely requiring used car dealers to tell the truth has led to some very unflattering characterizations of Congress in the media. *See, e.g.*, attached Herblock cartoon.

Moreover, as Senator Danforth recently pointed out, Congress has much more important things to do with its time than argue over the FTC's used car rule. In creating the FTC, Congress intended to set the broad limits of the Commission's authority and then leave the FTC, with its legal and economic expertise, to fill in the details. The legislative veto, as so dramatically shown by the rush to kill the used car rule, does a disservice to both Congress and the Commission. We respectfully request that it not be included in the new authorization bill.

VI. THE FTC'S BUDGET

The $68.1 million fiscal year 1982 appropriation for the FTC contained in the current continuing resolution represents a drop of 5 percent from the original $71.9 million for fiscal 1982 approved by the full House and Senate subcommittee, which itself represented a 20 percent reduction in real terms over the Commission's fiscal year 1978 budget. Moreover, the real decline in antitrust enforcement at the FTC is even more dramatic than the budget figures indicate: Chairman Miller has indicated that he will not challenge vertical or conglomerate mergers, vertical price fixing or other vertical restraints, or price discrimination under the Robinson-Patman Act; instead he will use the Commission's resources to intervene in other agency proceedings, to do economic reports, to aid business, and to challenge only the largest horizontal mergers. *See generally* FTC Transition Team Report, 127 Cong. Rec. § 10162-63 (Sept. 21, 1981).

In addition, at a time when the administration has committed itself to transfering power from Washington to the state and local level, Chairman Miller last year announced that he intended to close down all ten of the FTC's regional offices—where some of the Commission's most effective antitrust and consumer protection work historically has been done—and to centralize all the Commission's functions in Washington, D.C. Chairman Miller has announced that he intends to carry out the first installment of his plan in fiscal year 1983, by closing four of the FTC's regional offices.

We respectfully request that, at a bare minimum, the Commission's budget be maintained, in real terms, at the level originally approved by the full House and Senate subcommittee for fiscal year 1982, and that its ten regional offices remain open. To do less would both weaken antitrust enforcement and fly in the face of the administration's commitment to federalism.

Finally, we urge this Committee to provide for a private right of action under section 5 of the FTC Act. As the role of government is cut back it is more important than ever that people be able to protect themselves against unfair methods of competition and unfair or deceptive acts or practices. The FTC never has had the resources to protect all people against all such methods and practices; and it has even fewer resources today.

As you noted, Mr. Chairman, at hearings last year on "Consumerism in the 1980's," consumer protection today need not mean that the government must always protect consumers; sometimes the best kind of consumer protection is the kind that consumers can do for themselves. And perhaps the single most effective means of enabling consumers to protect themselves is to allow them—not just the government—to sue under section 5 of the FTC Act, just as individuals have always been able to sue under the Sherman and Clayton Acts. Whether the treble damage remedy should also be required under the FTC Act, and whether criminal penalties should also be assessed under the Act, are questions we believe this Committee should also consider.

In conclusion, we believe it is essential that the FTC reauthorization bill contain a provision allowing people and corporations—and not just the government—to sue for injuries they have incurred as a result of unfair or deceptive acts or practices or unfair methods of competition. Such a provision would dramatically enhance the ability of consumers to protect themselves. It would create no new federal bureaucracy. And it would not cost the federal treasury a cent.

Senator KASTEN. I hope that you did not mean to suggest that the last 2 days of hearings have been overwhelmed with business groups. Frankly, we have gone out of our way to try to have a balanced discussion of views and to try to have an open and full hearing on the different issues that we are faced with.

Mr. ANGOFF. Absolutely not, and I very much appreciate your giving us the opportunity to testify. I just do not feel that we are listened to sometimes quite as carefully as some of the other groups.

Senator KASTEN. I would like to ask Professor Gressman to comment to the point that Mr. Morrison made when he said that we might just as well authorize a committee or subcommittee or maybe even an individual elected official to veto agency rules, if you carry this out to its logical end. Could you comment to that point?

Mr. **Gressman**. Well, of course, you can carry any concept out to a logical extreme. I do not think, either to understand or to defend the kind of veto you have here by way of a concurrent resolution in both Houses, one has to be much concerned about the unlikely possibility that you could have one individual acting in the same role. Congress has never responded to this problem in that manner.

There are a vast number of veto provisions in the Code, and outside the Code, as I am sure the Senator is aware. There is a vast network of committee vetoes which operate all the time without benefit of statutory recognition. But those other situations may present quite different constitutional considerations than are involved in the two-House kind of veto in the Federal Trade Commission Act.

And frankly, my experience in participating in litigation where I have run into at least two types of vetoes, the one-House and perhaps some of the two-House variety, I am firmly convinced that you have to address each situation as it comes up, and not try to worry about excesses or extreme situations that may present entirely different considerations.

Senator **Kasten**. Thank you. I would like to thank all of the members of our panels for their testimony today. The record will remain open so that members may submit written questions to be answered for the record, and we are hopeful that the panelists would respond to those written questions within about 2 weeks' time.

Thank you again, and in particular, I thank the four of you for your participation on this important panel on the legislative veto. The hearing is adjourned.

[Whereupon, at 12:17 p.m. the hearing was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF MICHAEL PERTSCHUK, COMMISSIONER, FEDERAL TRADE COMMISSION

I am pleased to join in Chairman Miller's forceful opposition to special interest FTC exemptions for doctors, lawyers, dentists and other professions and quasi-professions. I wish also to commend Chairman Miller for the scrupulous fairness with which he delineates in his testimony those precise areas in which the four Commissioners are in agreement and those in which he speaks for himself. Because his testimony also contains several novel proposals whose implications have yet to be fully comprehended, I respectfully submit these separate comments so that the Committee can have the benefit of the full range of Commissioners' views on these issues.

DECEPTION

To the best of my knowledge, not a single advertiser, advertising agency or advertising medium or any of their trade associations has urged upon the Commission or Congress the statutory redefinition of deception. No previous Chairman or any individual Commissioner suggested it. It is my understanding that no other present member of the Commission supports it. Jeff Joseph, of the U.S. Chamber of Commerce is quoted as saying, "Everyone knows how far you can go with deception. We've had forty years of it." That the Chairman marches to his own drummer on deception by no means proves that he is wrong, but it is surely grounds for Congressional wariness.

As I understand the Chairman's proposals, before the Commission could act to halt a deceptive practice he would have us establish, subject to judicial review: (1) significant measurable injury to consumers; (2) a determination that the misleading statements were factual claims not "opinion"; and (3) in addition to demonstrating that the advertising had the propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising.

As a further gloss Miller would add that, in the event that the Commission could not establish that "reasonable consumers" would have been misled by the advertisement, the Commission might still prosecute the deception if it could prove that the seller actually knew or should have known that the advertisement was deceptive.

Given the enormous sophistication and subtlety of our marketing system and the glittering array of creative talent applied to motivating consumers to switch from brand X to brand Y, it is not surprising that the law of deceptive advertising has evolved slowly and painstakingly through generations of Commission decisions, subject to intense and careful scrutiny by the Appellate Courts including the Supreme Court. I believe that most legal scholars would affirm that today the law of deception is relatively well settled and provides solid guideposts for those practitioners who wish to remain in compliance with legal and ethical standards.

Into this settled legal environment, Chairman Miller's proposals would introduce great uncertainty and confusion. How does one measure the injury caused by a half-truth, a misleading claim, a distorted piece of evidence? How much is a lie worth to an advertiser? How much does a lie cost consumers? The value of truth and fair dealing is the mark of a decent civilzed society. Such a society does not stop to total up a balance sheet, weiging consumers' losses against business' gains when its citizens are being cheated, misled, manipulated and shortchanged.

In addition to requiring the Commission to measure the dollar cost of misleading statements, Miller would have the Commission look only at economic injury to consumers—assuming that could be measured. But advertisers themselves understand instinctively what the Chairman and like-minded economists appear to have missed—the damage caused by deceptive ads is not confined to consumers.

While the loss to an individual consumer duped into buying a product which is other than advertised may be only a few dollars, the advertiser's competitior may well be harmed in the millions of dollars. More importantly, deceptive ads, for example, misleading national brand advertising on network television, serve to undermine the credibility of all advertising, no matter how modest the cost of the product sold. Thus, the business community has a critical stake in assuring public confidence in advertising claims. How else can new or innovative products boasting enhanced performance reach mass markets?

This is why the very people one would expect to welcome Chairman Miller's efforts to unburden advertising are alarmed. That is why one advertising representative, hearing Chairman Miller express his belief that the Commission should not prosecute deceptive ads for inexpensive products, pleaded "Do we have to go back to the jungle?"

And it is why, in response to Chairman Miller's suggestion that the Commission's firm Advertising Substantiation rule might be excessively burdensome, the Vice President and Director of the Marketing Staff of General Foods wrote to him:

"Removal of substantiation requirements would remove the guarantor of advertising legitimacy on which consumers and advertisers now depend. It would place the ethical advertiser at a pronounced disadvantage: his messages would no longer be distinguishable from those of the unscrupulous. It would remove the base line of proper ethical conduct to which all advertisers are now required to adhere; diminish the ability of existing self-regulatory mechanisms to resolve conflicts between competitors; force the consumer and the ethical advetiser to bear the penalty for unscrupulous advertising; and, promote chaos in the marketplace."

I have also attached for your information an article by Advertising Age Washington Editor, Stan Cohen, a steady voice for sound regulation in the advertising community, entitled, "Consumer Safety Net Starting to Unravel."

I am at a loss to understand why Chairman Miller feels that it is essential that Congress prohibit the Commission from proceeding against deceptive "opinions." I know of no case that the Commission has brought challenging opinions except for those cases in which the Commission has alleged that opinions such as those of scientific experts were designed to lead consumers to believe that the opinion was backed by expert knowledge and experience. If Dr. Michael DeBakey, the famed heart surgeon, were to appear in a cigarette ad claiming that in his measured opinion as a surgeon it was his judgment a particualar cigarette cured cancer, Miller's amendment would appear to place such opinion testimony beyond the reach of the Commission's policing powers. I simply disagree that there is any sound public policy advanced by doing so.

The Chairman's proposal to incorporate a standard of "reasonable" consumer behavior introduces yet another lever for legal mischief. In allocating the Commission's increasingly scarce law enforcement resources, it ordinarily makes little sense to protect consumers against deceptions which are transparent or unlikely to deceive any but the willfully gullible. But incorporating such standards into the Commission's administrative proceedings and appellate reviews as a matter of substantive law would insure that the hearings would dwell, not only on the normal evidence that an advertisement has the capacity to deceive consumers, but also would include clashes of expert psychologists and other behavorial scientists over the arcane question of whether consumers—who might, in a weak moment, be taken in by the deception—should have known better.

Finally if the challenged advertising was directed at "vulnerable groups"—the poor, the elderly, and the uneducated—who might fall through the statutory category of "reasonable consumers," Miller would still give the Commission a shot at protecting them from deception if we are able to prove that the advertiser actually intended to deceive or that the reasonable advertiser should have known that his ad was deceptive. A mens rea requirement has never been an element of deception under Section 5, and appropriately not. The FTC Act is not a criminal statute. It does not punish the sinner, it simply seeks to protect the consumer. Intent is irrelevant to whether consumers may be injured and, consequently, to whether a company should be ordered to cease and desist from deceiving the public. Moreover, intent is enormously difficult to prove. Therefore, while Miller's proposal purports to provide special protection for vlunerable groups, the impact of his proposal would leave such groups far more vulnerable to exploitation than under present law.

Throughout the history of the Federal Trade Commission Act, Congress and the Commission have sought simple, effective, clear guideposts, both to the advertising community and the courts to police deceptive advertising. By 1968 the legal hurdles to effective law enforcement against deceptive advertising had so emasculated the FTC that the American Bar Association appointed, at the request of President Nixon, a blue ribbon panel to examine the Commission's frailties. It concluded that, unless the Commission was able to develop and pursue effective law enforcement techniques against such practices, Congress should seriously consider shutting the Commission down. Responding to this challenge, four successive, conservative Republican Chairmen (Caspar Weinberger, Miles Kirkpatrick, Lewis Engman and Calvin Collier) successfully led the Commission through the development of an effective law enforcement program against deceptive practices. Quite simply put, Chairman Miller's proposals would go a long way toward dismantling their work and returning the Commission to those (pre-feminist) days when it was scorned by consumers and business alike as the "little old lady of Pennsylvania Avenue."

UNFAIRNESS

This appears to be open legislative season on rewriting the Commission's authority under Section 5 of the basic FTC Act to police "unfair acts or practices affecting commerce."

The Chamber of Commerce would simply abolish the authority. Representatives of the advertising industry would only abolish it for advertising. The NAM and others seek to do what Congress refused to do in 1914—write into the law a rigid laundry list of specific prohibited practices. A majority of the Commission support a more modest proposal—enshrining in legislative language a standard of unfairness based upon the Commission's December 1980 Policy Statement. I respectfully disagree and urge Congress to leave the statute as is.

In February, 1970, the Chairman of the FTC, Caspar W. Weinberger, responded to a request from Congress for the Commission's views as to the desirability of redefining unfair acts or practices. Speaking for an unanimous Commission, Chairman Weinberger wrote:

"The Commission has given this matter considerable study and has concluded that it is impractical to attempt to categorize the acts of practices which are unfair or deceptive to consumers. Any listing that is complete today would be incomplete at the time of enactment into law. If complete at the time of enactment, it would soon be outdated through the ingeniousness of the unscrupulous businessman.

"A further difficulty, which would be encountered in attempting to define or categorize unfair or deceptive acts or practices for the purposes of this bill, is the probability that it will take years of litigation and consequent judicial interpretation to ascertain with any degree of certainty each category, or conversely, the acts or practices not included within the scope of the bill."

* * * * * * *

In December, 1980 the Commission responded to requests from Congress for a formal policy statement articulating the standards guiding the Commission's application of its "unfairness" authority. The product was a meticulous restatement of the law of "unfair practices" as it had been developed by the Commission under the supervision of the courts through six decades of legal evolution. The statement made it crystal clear that, contrary to simplistic criticisms, the Commission's unfairness authority was not what any three Commissioners believed to be "unfair."

To the best of my knowledge no critic of the Commission has identified any final Commission rule or Commission order necessitating or justifying the radical restructuring of the Commission's fundamental legal charter. I know of no arguments that, had the Commission operated under any of the proposed new standards, any previous case or rulemaking would have reached a more felicitous conclusion.

The Commission's unfairness authority has proved time and time again an important safety valve for the predatory overreaching of sellers that does not fit neatly within the confines of deception. And, just as the Chairman has aptly argued against the carving out of exemptions for specific industries, I see no justification whatsoever for carving out an exception to the Commission's unfairness authority for the advertising industry.

I do not know of any public clamor which suggests that advertising has reached such a state of purity that there no longer exists a possibility that an advertiser will attempt to sell his product through psychological manipulation or other means, not technically deceptive, but severely damaging to the health or economic well-being of consumers. As Chairman Packwood has forcefully indicated would Congress really want to deprive the Commission of the opportunity to halt advertising campaigns which promoted cigarettes, beer and over-the-counter drugs as essential to the health and sexual well-being of the adolescent girl or boy? Or what about showing a young boy riding a power mower in the street?

LEGISLATIVE VETO

Without further embellishment, I should indicate for the record, that I remain firmly opposed to legislative veto. Now, with the benefit of two years of experience under the FTC Improvements Act of 1980, it is plain that the device has served as little more than a spawning ground for business PACS and has consequently placed a cloud on the integrity of congressional decisionmaking. As Congress demonstrated in responding to the Commission's initiative in children's advertising, the legislative veto is not necessary to enable Congress to make its will known and felt.

PUBLIC PARTICIPATION FUNDING

Why this modest program, designed to fund at a most limited level the voice of consumers and small business interests, strikes terror in the hearts of the Chamber of Commerce and NAM has always baffled me. I had never thought that the spirited advocacy of differing sides of regulatory issues posed a threat to a democratic society. In any event I remain an enthusiastic supporter of this concept, especially since I have seen it work in sharpening a debate before the Commission and enhancing the Commission's own decisionmaking process. The efforts to eliminate the program can perhaps best be viewed as a terminal overdose of ideological distrust of participatory democracy.

REAUTHORIZATION FUNDING

The present authorization for Fiscal Year 1982 is $80 million, compared to a proposed appropriation for Fiscal Year 1983 of $60.8 million. These figures tell us much about the Reagan administration's plan for the FTC and other non-defense agencies. I support a continued authorization level of $80 million for the next three years with the Appropriations Committees determining how much of this is available in the budget. Fortunately, the citizenry at large shows no signs of support for retrenchment in antitrust and consumer protection law enforcement.

CONCLUSION

In fairness to Chairman Miller, his reforms are not offered in the name of business relief. Chairman Miller argues eloquently that his reforms will serve the greater consumer interests.

Yet every survey of citizen opinion which I have seen reveals that the public is not only demanding continued consumer protection, but that strengthening the policing of advertising stands at the very top of the list of consumer demands.

Opinion Research Corporation reported in January, 1981: "Advertising is clearly the activity where large U.S. Corporations are most vulnerable to public criticism. Not only do significant proportions of people call for more government involvement in this area, they also are more likely to give companies poor ratings for the kind of job they are doing to provide truthful and tasteful advertising than for any other corporate activity directly related to the consumer." A poll in Roper Reports, published in August 1981, shows 74 percent of the public believes it is "largely true" of American business that it "hoodwinks [the] public through advertising," up 5 points from 1975.

Make no mistake of it. Amending, redefining, and complicating the Commission's statutory authority would serve the interest only of those fringe advertisers tempted to shave the truth, dissemble, spawn half-truths, and make claims based on flimsy, hoked-up tests.

Chairman Miller has argued that the healthy condition of self-regulation in the advertising industry today justifies the withering of FTC's law enforcement presence. But quite the opposite is the case. There was only token self-regulation until the Commission got tough and effective. Only then were those members of the advertising community who held themselves to the highest ethical standards able to convince their competitors—far more vulnerable to Commission action—to join in an effective self-regulatory program. The Commission's aggressive action alone provided the opportunity for the highest ethical practices to become the standard.

Section 5 of the Federal Trade Commission Act has stood intact for more than 40 years. In those instances in which the Congress has been displeased with Federal Trade Commission actions, Congress has found ample opportunity to make its will known and heeded. At the same time as a fundamental charter of truth and decency in the marketplace, the FTC Act has withstood the test of time. If it isn't broken, don't fix it.

[From Advertising Age, Mar. 8, 1982]

CONSUMER SAFETY NET STARTING TO UNRAVEL

(By Stanley E. Cohen)

WASHINGTON.—Exactly a dozen years ago this week, former President Richard Nixon gathered in the White House Family Theater a galaxy of tough law enforcers he had recruited to deal with consumer problems that kept Ralph Nader's name on Page 1.

Advertising flimflam was high on the list. In those days it was common even for respectable advertisers to make claims they couldn't substantiate and use TV demonstrations which really weren't proving anything. Now that advertisers are doing nicely without this sort of hocus-pocus, it is painful to recall how the industry leaders of that period indignantly defended these practices.

Among those at President Nixon's meeting was Caspar Weinberger, imported from California to help set things straight. Mr. Weinberger was probing for new concepts of marketplace fairness.

It was several years before the adoption of a rash of consumerists laws embellished FTC power. With only the basic FTC law as his source of power, he had begun issuing industrywide rules, including a rule requiring posting of octane ratings on gasoline pumps, and rules banning the distribution of unsolicited credit cards and merchandise.

Under chairman Weinberger and his immediate successor, Miles Kirkpatrick, the basic Federal Trade Commission law, written long before modern marketing concepts were visualized, was adapted to changing need. New moral and legal concepts were woven into a safety net protecting the public and the honest businessman from the marketplace perils of the 1970s, and these efforts were widely praised as proof that, given good leadership, a tired old bureaucracy can be rejuvenated.

Now a dozen years later, a different political tide is running, and that safety net is beginning to unravel. Congress must act before Sept. 30 to keep FTC operating. A vigorous drive has developed to curb FTC's reach, and this broadly based movement, supported by Reaganites at FTC as well as outside critics, could lead to a new double standard in the policing of advertising that has far-reaching implications for the ad business.

In place of Caspar Weinberger, who looked for previously unsuspected power in the basic FTC law, the commission now has a chairman, James Miller III, who searches for ways to narrow the commission's authority. for chairman Miller, it is not merely a matter of pulling back from the consumerist legislation of the 1970s. His target is the time-tested language of Sec. 5 of the basic FTC act—the mainspring of FTC power, and the resource that was used by chairman Weinberger and chairman Kirkpatrick to weave that safety net.

Once again there are meetings to discuss the future of FTC. At the American Advertising Federation, ad industry leaders, still smarting from the fight over a children's advertising rule, want the word "unfair" ripped out of the law. The Reaganite chief of FTC's bureau of consumer protection offers guidance. Eliminating "unfair" really won't meet their problem, he tells them. What they need to do is narrow the commission's authority over "deceptive" ads.

In the Voluntary Action Room of the U.S. Chamber of Commerce, a coalition of industry representatives meets to develop a list of amendments shrinking the reach of Sec. 5. FTC enforcement of laws against unfair and deceptive acts and practices would be restrained by requiring more burdensome standards of proof, akin to those required under the Sherman Antitrust Act.

While FTC would continue to police "unfair" as well as "deceptive" ads, the coalition proposes to impose a cost/benefit test. Under this concept FTC could act only against ads which "cause or may foreseeably result in substantial injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition."

The coalition and its allies among the Reaganites at FTC is candid about its intent. They hope to get FTC off the backs of business, unless it has a solid case and the stakes are high. Superficially, at least, this is a reasonable objective, particularly for businessmen who feel they have been subject to unwarranted abuse. But as one who has written about these issues for 40 years, I suggest this is a concept that ignores the lessons of experience.

FTC was created in 1914 because 25 years of experience with the Sherman Act persuaded the bipartisan political leadership of that day—President Woodrow Wilson, and former Presidents Theodore Roosevelt and William Howard Taft—that a more effective system was needed to deal with trade practice problems. In every-day marketplace unfairness, it is frequently impossible to get the kind of evidence needed in Sherman Act situations. If skullduggery was to be eliminated, the enforcing agency would need authority to act on the basis of a less demanding standard of proof.

The effort to impose a cost/benefit test on FTC advertising cases distorts FTC's role in the advertising field. Cost/benefit is, of course, a legitimate consideration in selecting advertising cases, and the commission traditionally takes it into account. But cost/benefit is only one consideration, and not necessarily the most important one.

FTC's duty is not to the defrauded consumer alone, but to the marketplace itself. The commission is less concerned about the size of the injury than it is about the morality of practices that prevail. It is worth noting that the safety net woven by Caspar Weinberger and Miles Kirkpatrick is made from cases that might not have been possible if they had to contend with the cost/benefit barrier currently under consideration.

Only nominal consumer injury was caused by advertising for Palmolive shave cream, Pfizer's Unburn and Listerine. Yet the ban on phony TV demonstrations, the ad substantiation doctrine and the concept of corrective advertising established by these cases moved advertising ethics from the flim-flam that prevailed in the 1960s to the laudable standards that exist today.

Before going further down this road, I hope the leaders of the advertising business will soberly consider the consequences. My experience persuades me that advertisers who are scrupulous in respecting the rights of their customers and competitors have little to fear from FTC. Yet they are the ones who have the most to lose if loopholes are inserted in the law that make it more difficult for FTC to deal with less socially responsible advertisers.

With the cost/benefit test in place, there will be no help from FTC when companies marketing small-ticket package goods items face less socially responsible competitors using dubious advertising techniques. With FTC removed from the picture, the less scrupulous small-ticket package goods marketer is also free to thumb his nose at self-regulation.

The cost/benefit concept leads to two-tier morality, with tough FTC justice for the auto industry, the appliances industry and other big-ticket items, and sanctuary for the small-ticket package goods marketers. But in the end, as the cumulative impact of unpunished misdeeds by small-ticket advertisers erodes public confidence in advertising, and public respect for advertising people, the entire advertising business bears the consequences.

Cost/benefit as a statutory test would be less objectionable if there was reason to believe the full meaning of "cost" and "benefit" were understood. For example, will cost/benefit take into account the social disarray that develops when consumers feel they are systematically abused? We are in an era when advertisers are skilled in using the latest social science knowledge to penetrate consumer defenses, and a new media mix is emerging opening the ways for selling techniques yet to be invented. What will the ultimate cost be if FTC lacks the reach to deal with problems as they develop?

And how do we measure "benefit"? Palmolive Rapid Shave, Unburn and Listerine led to a new ethic which encourages consumers to respect advertising people and trust in advertising. Advertisers get a bigger bang for their advertising buck. Prices are lower because effective advertising holds selling costs down. How do these valuable considerations survive once the law is amended so FTC deals only with advertising cases where the injury to consumers exceeds the countervailing benefits?

STATEMENT OF THE AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS

Mr. Chairman, the AFL-CIO appreciates this opportunity to present its statement on legislation reauthorizing funds for the Federal Trade Commission. While the Federation is not an expert on the laws enforced by the FTC, nor the Commission's experiences in enforcing them, we know the FTC well enough to be concerned about proposals before you to reduce the Commission's authority to eliminate and prevent deceptive and unfair trade practices or restrict its ability to investigate and prosecute anti-competitive practices.

In this period of high inflation and high unemployment, the members of our unions—like most consumers—need more, not less, protection in the marketplace. Because of high rates of unemployment among primary wage earners, fewer households today have a professional homemaker that can spend substantial amounts of time assuring that all of the family's purchases are based on comparison shopping or sufficient information to assure a wholly rational choice among products. In short, our members cannot afford to find out too late—after they have spent their hard earned dollars—that the products they have purchased do not perform as promised.

It is popular to say today that the American people want "less big government" in their lives, but we have heard no clamor for less federal law enforcement in the area of consumer protection. In fact, the consumers of America want someone policing the marketplace. We want some assurance that we can believe what we are told about products in TV ads. We want more information about the products we buy, and that such information be reliable. In other words, we want the government to assure some reasonable level of credibility in advertising.

The power of the FTC to acquire advertisers to have a "reasonable basis" for their product claims should not be put in jeopardy by a narrowing of its authority over unfair or deceptive practices, or by legal requirements that it weigh the "costs and benefits" of its actions. This would mean less protection for consumers.

Similarly we oppose any effort that would diminish the ability of the FTC to protect consumers from abusive practices, including those that might not be called deceptive. Business entities be they large or small should not be able to base their sales programs on high pressure tactics, or appeals to emotional vulnerabilities. Nor should businesses be allowed to harass a worker when he or she is economically vulnerable—when they are laid off and fall behind on installment payments to the furniture company. Then they need protection from harassing telephone calls in the middle of the night. Finally, of course, we want someone to protect workers and indeed all consumers from simple fraud.

I don't think anyone has suggested that the FTC should no longer be allowed to sue companies for fraud. Marketplace fraud is not only injurious to consumers, but, as well, jeopardizes the credibility of the business community and as such is bad for business. Yet, changes to the FTC Act now being proposed could make it much harder for the FTC to pursue, investigate and prosecute fraud. It is obvious that if the Commission is forced to satisfy more cumbersome legal requirements when it brings a case, such as showing that a certain percentage of "reasonable" consumers were deceived by an ad or that the advertiser "knew" that his claim was false, the FTC will be unable to bring as many cases or try them as quickly.

Why, then, are there rather drastic proposals before the Committee to change the FTC Act? Perhaps it's because the advertising industry and others were furious when the FTC proposed in 1978 to do something about potentially harmful advertising aimed at small children. Yet, what did the FTC actually do? On children's advertising the FTC issued a staff report and closed its rulemaking. In short, in this controversial area, the Commission simply contributed useful information to the public debate on an issue that affects millions of Americans. This is no reason for wholesale changes in important aspects of the basic authority of the FTC.

Besides the advertising industry, the networks, sugar, candy and tobacco manufacturers, the oil companies that were the subject of an FTC anti-trust investigation were all agitated by an agency doing its job. A quick glance at the recently released report on the FTC's activities for fiscal year 1980, shows how well the FTC was protecting consumers and small business interests in chalking up an impressive record of consumer protection cases. In doing so, the agency also alienated a range of other corporate and business interests who were the subject of FTC investigations, rulemakings or litigation. For example, the FTC negotiated orders with companies that required them, among other things, to:

give consumers their money back when they default on layaway purchases;
stop billing consumers for unordered merchandise;
familiarize employees how to comply with the Equal Credit Opportunity Act;
terminate fraudulent land sales schemes;
replace rusted fenders in automobiles and prevent unsubstantiated claims for a purported fuel economy device;
correct the unsafe installation of woodburning stoves;
stop depicting unsafe riding habits in ads for bicycles; and
disclose the relative effectiveness of certain contraceptives, while stopping the performance of dangerous hair implants.

In addition, the FTC negotiated civil penalties against companies for:

adopting bait and switch practices;
using abusive language to consumers in telephone calls about delinquent debts;
discriminating against Blacks, Hispanics and women in granting credit;
refusing to allow consumers to cancel magazine subscriptions;
adding illegal fees to consumers debts; and
employing other unfair or deceptive practices.

In litigated cases, the Commission ordered an auto dealer to refund to consumers the surpluses from the sale of repossessed cars, required a national retailer to stop making false claims about the performance of its dishwashers, and stopped a vocational school from misrepresenting employment prospects and potential earnings of graduates.

These are only some of the activities in an impressive record of consumer protection by the Bureau of Consumer Protection. Is it any wonder that business groups have lined up to emasculate the consumer protection authority of this agency?

The FTC Bureau of Competition was just as busy in the anti-trust area and its work, of course, also results ultimately in benefits to consumers in the form of increased competition and lower prices. The benefits to consumers are perhaps most obvious in cases involving restraints on cost-containment programs in the health care sector and in other overt price-fixing cases.

With respect to FTC anti-trust authority, the AFL-CIO would like to take this opportunity to state for the record its opposition to S. 1984 which would have the effect of exempting from FTC study, prosecution and rulemaking anti-competitive practices engaged in by so-called professions. When this issue arose in 1980 the AFL-CIO opposed it as an amendment to S. 1991, the FTC reauthorization bill. The basis of our opposition stems from our belief that the FTC should have the power to prevent anti-competitive or fraudulent conduct by such professions as doctors, lawyers, dentists and others, particularly when such behavior discourages price advertising, fee competition and development of para-professional services, health maintenance organizations and other lower-cost alternatives.

Regarding health care, as members of the Senate Commerce Committee are aware, the AFL-CIO has been in the forefront in both the collective bargaining and legislative arenas in advancing low-cost health care alternatives such as HMOs while some of our affiliated unions have worked with their management counterparts to develop cost containment programs for negotiated fringe benefit plans. In several instances the FTC has undertaken anti-trust lawsuits against the medical profession for engaging in boycott activities designed to deter or destroy these health care mechanisms designed to reduce spiralling medical care costs.

It seems to us, therefore, that if the Congress is truly serous in its concern for the problem of inflation which in part has been driven upward by the ever-increasing cost of health care, then it will not strip the FTC of its anti-trust authority in this area. We are hopeful, based on the public statements of Chairman Kasten, that he will continue to resist any such diminution of FTC anti-trust authority in the health care or any other area.

A review of the FTC's accomplishments has convinced the AFL-CIO that the agency is performing a valuable service not only to our members but to all American consumers. We urge the members of the Commerce Committee not to make the FTC's job more difficult! Changes to the FTC Act that would make litigation more complex, or that would exempt special interst groups from the FTC's scrutiny, are not in the interest of the working people of this country.

STATEMENT OF NATIONAL INDEPENDENT DAIRY-FOODS ASSOCIATION

The National Independent Dairy-Foods Association (NIDA) is the largest trade association of independent dairy processors and distributors with a nationwide membership. Members are predominantly small businesses. Many are family owned proprietorships, partnerships, and corporations.

One of the principal objectives of the members, as expressed through NIDA, is to seek to gain equity in the processing, manufacturing, and marketing of fluid milk, cheese and other dairy products and allied foods. NIDA strongly endorses a marketplace for our members with as much freedom to compete fairly as possible, with a minimum of restraints, whether now imposed by cooperative monopolies or governmental regulations, or a combination of both.

—NIDA supports and endorses the continuation of antitrust authority in the Federal Trade Commission, and its present application to agricultural cooperatives.

—NIDA opposes any diminution of FTC antitrust authority over agricultural cooperatives.

—NIDA firmly believes that the FTC should have authority to investigate, make reports, and take appropriate actions consistent with the Capper-Volstead Act, the Agricultural Marketing Acts, the Clayton Act, and the FTC Act, as amended, in regard to any conduct or practices of cooperatives, separately or in federations or in connection with any governmental program.

—NIDA firmly opposes the creation of any new antitrust immunity or the enlargement of any existing antitrust immunity for agricultural cooperatives.

The FTC has a definite and important function in antitrust enforcement. Small businesses have traditionally looked to FTC for the type of enforcement actions which "clean up" various markets cluttered with trade restraining practices. The dairy industry is a prime example of an industry cluttered with trade restraints and monopoly practices by regional dairy cooperatives. This situation has developed, in part, due to the permission of Congress and the design of the Department of Agriculture. It has also resulted from the one-sided enforcement of the antitrust laws by the FTC and the Department of Justice against the national and regional dairy corporations. This one-sided enforcement policy created a vacuum which was filled by aggressive dairy cooperatives operating under the shield of Capper-Volstead.

During the last five years USDA has promoted an unbridled merger trend among the various daily cooperatives. There has been an unparalleled wave of acquisitions of proprietary dairy facilities by these dairy cooperatives. This merger trend has resulted in concentrations of power in both milk production and manufacturing.

The Federal Trade Commission has been extremely prudent and overly conservative in using its antitrust authority to curb numberous violations of the Clayton and Federal Trade Commission Acts by agricultural cooperatives. It is not the radical body which its enemies have asserted over the years. FTC cases involving cooperatives have been few and far between. Nevertheless, its continued authority is essential in the dairy industry.

The few recent FTC actions have, and are, providing a little sanitizing action to an industry which has seen thousands of small independent businesses swept aside by the powerful forces of regional cooperatives, national retail chains, and excessive market order regulation. The marketing orders protect and enhance the dairy coops' market power, while USDA is actively promoting further mergers. This system is designed to reduce competition in the dairy industry, at the expense of small businessmen and the consumer. The major policy executives at USDA have used the Secretary's power to encourage the growth of multi-state dairy cooperatives while discouraging the independent cooperative, dairy farmer and handler.

The FTC has challenged monopoly in *FTC* v. *Sunkist Growers Inc.* FTC DKT 9100; (*Sunkist* v. *FTC*, 1979-1) Tr. Cases § 62,469; 464 F Supp. 302) in the California markets for fresh lemons, oranges, and lemon products through the use of restrictive agreements and exclusive dealing contracts with packing houses. In the dairy industry FTC currently is challenging the powerful Southeastern Dairy Cooperative's acquisition of a major non co-op competitor in *FTC* v. *Dairymen, Inc. and Mumford Inc.* DKT 9143. In this action the issue of FTC's jurisdiction and procedure has been upheld by the Courts. (U.S.D.C., KY). Its right to proceed normally, without being "ham strung" by a warped interpretation and application of Section 20(a) of the FTC Improvements Act of 1980 has been upheld. Neither of these FTC actions is a threat to the survival of cooperatives which serve the true interests of their members by use of lawful business practices.

In the matter of *Western General Dairies, Inc.* (consent order to cease and desist, File No. 7610004, February 22, 1982), the FTC has acted to halt the destruction of competition in the dairy industry in the mountain states.

The matter is reported in this manner: "Western General Dairies, a dairy cooperative, agreed to change its contracts to permit a member to sell raw milk after leaving the association, under an FTC proposed consent order. The cooperative will also offer non-discriminatory prices and services to all of its raw milk and dairy product customers. * * *

"The Commission charged that Western General Dairies suppressed competition in the production, sale and distribution of raw milk and in the sale and distribution of dairy products. This was allegedly accomplished by: offering advantageous prices and credit terms to some dairy products purchasers but not others; spreading derogatory information concerning the creditworthiness of competitors in the sale and distribution of dairy products, and restricting the sale or transfer of base by members desiring to leave the cooperative by prohibiting such members from producing Grade A milk." (CCH) Tr. Reg & Regs § 21910.

Attached to NIDA's comments are the statement of National Association for Milk Marketing Reform (now part of NIDA) concerning the size and financial strength of various agricultural and supply cooperatives in 1978-79; and a current article from USDA's Farmer Cooperatives reflecting the size and growth of super cooperatives; and selected pages from USDA's Federal Milk Order Market Statistics for December, 1981.

The NAMMR statement "Look at Who the Agricultural Cooperatives Are and Why They Seek Further Immunity From Antitrust" which was prepared in January, 1980, is pertinent to the current consideration of the Committee of reauthorization for the FTC. The November, 1981, article "Top 100 Dominate Business Scene, Sales Hit $50.3 Billion by 1980," authored by three Agricultural Cooperative Service (USDA) economists, illustrates the explosive growth of these agri-corporations.

Meaningless comparisons by the authors with annual sales of Texaco and Exxon and the size of Shell Oil's assets can be disregarded for obvious reasons. They are similar only in that they are corporations, one tax paying, the other non tax paying. Agricultural cooperatives cannot be compared with multi national oil companies—they are in totally different industries (except some supply co-op operations), and do not compete in broad markets.

The statistics in USDA's "Cooperatives in Federal Milk Order Markets" (attachment 3) show the continuing concentration in the dairy industry of the dairy cooperatives. The small declines do not affect the picture. For example (4) page 41: "For all Federal Order markets combined, the four largest cooperatives accounted for 32.2 percent of all producers and accounted for 30.5 percent of the total milk marketed under Federal Orders." Also note (7) page 42, "Of the total number of Federal order producers belonging to cooperatives in December 1980, the largest cooperative in each market accounted for 51 percent of these producers. Producers belonging to the largest four cooperatives in each order accounted for 79 percent of the total cooperative membership in Federal order markets."

The Congress should recognize that the absence of a national dairy policy coupled with an unbalanced pro cooperative policy by USDA aimed at establishing two super regional milk cooperatives—one East and one West of Mississippi—calls for close scrutiny by an independent agency, the FTC. The Commission should be directed to annually review and report to the Congress on the markets in milk to determine whether there may be an unwarranted economic concentration in either the production and supply or in the marketing of the nations's milk.

NIDA takes the position that Section 20(a) of the 1980 Improvements Act (Pubic Law 96-252, Sec. 20, 94 Stat. 393) is superfluous and unnecessary. It simply states the preexisting law. Section 20(b) should be amended to mandate an FTC study of agricultural marketing orders from the antitrust viewpoint as they affect trade, commerce and business. Those studies and subsequent reports to Congress should parallel present USDA market order studies such as the milk marketing and surplus study required by Section 107 of the 1981 Farm Bill. The necessity of the studies results from the fact that producers are not merely family farmers, but the owners of large scale food processing and manufacturing businesses. USDA, as evidenced by its January, 1982, Guidelines for Fruit and Vegetable Orders, is simply not equipped to handle such studies alone.

The FTC must continue to have authority to investigate and prosecute those unlawful activities of agricultural cooperatives which are not exempted by Capper-Volstead.

The current active cases involving dairy cooperatives must not be disrupted by special interest legislation.

The long and well documented record of abuses and predatory behavior by the super regional cooperatives justifies the reauthorization by the FTC's jurisdiction over agricultural cooperatives.

LOOK AT WHO THE AGRICULTURAL COOPERATIVES ARE AND WHY THEY SEEK FURTHER IMMUNITY FROM ANTITRUST

Farmer Cooperatives are big business in not only the marketing of many basic products and commodities, but they have become the processors and refiners—they are almost the total suppliers of all goods and services to large segments of our population. Co-ops are agribusiness corporations with billions of dollars of assets and multibillions of dollars in sales.

Below is a partial list of some of the biggest:

	1978 sales (billions)	1978 Fortune 500 standing
Farmland Industries	$3.215	91
Associated Milk Producers Inc. (AMPI)	1.772	163
Agway, Inc	1.700	173
Land O'Lakes, Inc	1.490	194
Gold Kist, Inc	1.290	217
Dairyman, Inc	[1] 1.100	258
CF Industries	.671	342
Sunkist Growers, Inc	[2] .500	
Midland Cooperatives, Inc	.404	483

[1] Estimate of NAMMR.

[2] FTC Docket #9100

Source: Fortune 500

Why do they need your vote to extend their Capper-Volstead exemption by taking away the FTC's funds and authority to even do fact-finding studies? Why do they need this when the FTC bill contains a legislative veto provision? Because some of these giant multistate corporations want to expand to monopoly size in regional areas. Those that dominate their markets now want no interference with their power to control production, eliminate their independent competition and to fix prices.

Why do these giant agribusiness co-ops fear competition from smaller farmer-owned cooperatives or free independent farmers when their markets are regulated by Federal market orders? Because they want to continue to use their market dominating power to extract from the consumers premium prices which exceed the Federal order prices as in many of the nation's milk markets.

The 700 million dollar dominating Southeastern milk co-op extracted a premium of $.75 per cwt. in Atlanta in November 1978 and pushed this to $1.38 in November 1979 as it increased its market power. The premiums are $1.23 in Nashville and $1.13 in Miami in November 1979. It is the consumer who ultimately pays the higher prices in retail stores (milk is well over $2.00 per gallon now).

If the Secretary of Agriculture has sufficient authority to stop co-op antitrust abuses under Capper-Volstead, why hasn't a single action been brought by him since 1922, in spite of the fact that numerous U.S. and private cases have been prosecuted?

The National Association for Milk Marketing Reform submits that the Secretaries have been extremely understanding and benevolent traffic officers and simply look the other way when co-ops travel the antitrust road. We doubt that the Secretaries understand antitrust violations and their effects on consumer prices because they have known, or should have known, that these are FTC and Justice functions.

We hope that the Senate will instruct its conferees to eliminate the Andrews Amendment to HR-2313.

STATEMENT OF THE AUTOMOTIVE SERVICE COUNCILS, INC.

Automotive Service Councils, Inc. (ASC) is a national trade association, a federation of State incorporated councils which are comprised of automobile, truck and other vehicle repairers. ASC is a not-for-profit corporation chartered and headquartered in Illinois. Its 5,000 members are all small businesses, some incorporated, but most are individual proprietaries or partnerships. Approximately 2,500 ASC members are engaged in the repair of crash damaged vehicles involving sheet metal and structural restoration work in competition with each other and similar repair facilities of franchised automobile and truck dealers.

ASC members, as small business enterprises, function in an industry which is frequently manipulated and often dominated by powerful automobile casualty insurance corporations which control 90 percent of the cash flow to the collision repairmen. Their claims settlement procedures usually dictate the methods of repair, quality, total sums and terms of payments.

ASC strongly opposes any special exemption for the insurance industry from any current antitrust jurisdiction in the Federal Trade Commission. ASC endorses continued antitrust authority for the FTC.

ASC favors an amendment to FTC's authority to, not only allow it, but to direct the FTC to study anticompetitive practices of insurance companies—notwithstanding the McCarran-Ferguson Act. The FTC should have the power to take appropriate action for the reason that none of the States have effectively or appropriately regulated insurance company trade restraints in the services provider industries.

The casualty insurance industry's purpose in extending their limited exemption from the application of the United States antitrust laws is not compatible with a free competitive marketplace. Their interest in private price fixing functions is not in the best interests of the more than 100 million insured motor vehicle owners. They are at cross purposes with our nation's free market philosophy. Giant insurance companies are privately regulating and controlling the business activities of the 40,000 independent and 20,000 franchised new car dealers engaged in the automotive collision repair business.

ASC members have historically opposed any enlargement of the McCarran-Ferguson Act (15 U.S.C. § 1012(b)) antitrust exemption. They recognize that broad enforcement of all antitrust statutes, federal and state, ultimately serve their common good. If these laws are not always a kind of charter of economic freedom, their enforcement frequently deters abuses of that freedom by the powerful.

Through their national organization, ASC members have a vital interest in this legislation. ASC favors a balanced enforcement of federal antitrust laws. This means no special immunities from any federal enforcement authority.

ASC has other concerns relating to the misconceptions about risk spreading and underwriting by the automobile casualty insurance companies and the third party provider relationships. This should be examined by the FTC.

The real and present danger of failing to provide basic FTC authority allows the opening and expanding of possibilities that all cost containment activities of insurance companies could escape antitrust scrutiny. The autobody repair industry and ASC's members may remain subjected to even more pervasive private regulation and domination by the insurance companies.

Insurers use the argument which ASC rejects, that society benefits from cost containment which justifies price fixing mechanisms. The Supreme Court clearly disposed of this argument in the *Royal Drug* case. ASC argues that the cost containment position is equally without support in law and fact. The collision repair industry is penalized to the extent of depressed wages, earnings and the inability to acquire the needed modern equipment to perform quality restoration of vehicles to their pre-crash value. This is largely caused by the insurer's cost containment. But the real victims are the vehicle owners who collectively suffer multibillion dollar losses in depreciated values of vehicles which are cutrate repaired, and not restored to the value prior to being damaged. No one argues for increased automobile or medical insurance premiums as being beneficial to society. However, cost containment price fixing exacts its toll. A competitive market free of private regulation is the best means for insureds to receive the services they want, and to which they are entitled under their contracts of insurance.

The insurance policy—the contract between the insured and the insurer—should on its face contain the specific limits to which the insurer is willing to agree to reimburse the insured. If the insurer wishes to cost contain his risk of loss, the insurer should be specific in the policy, otherwise the deductible stated therein becomes a floating, variable amount—depending upon the whims, policies and claims settlement procedures adopted by the insurance company.

The amount of loss to the insured should arise from the competitive costs for a quality restoration. Competition, not private regulation or cost containment should be the discipline that determines the amount of loss to be compensated.

Claims adjusting is designated by the insurance industry as the business of insurance that Congress exempted in McCarran-Ferguson. This is not what Congress described as an insurance practice exempted in favor of State regulation. ASC believes that if this were ture, it would be a license to the State insurance regulators to expand their authority to every conceivable function relating to the business of insurance. Claims adjusting is not essential to the auto casualty industry. The internal function of insurance personnel in handling claims is essential but not the use of "preferred shops" adhering to "approved rates" by auto insurers. Computer data on ranges or averages of losses is readily available. Any competent insurer has access to quantities of cost information from a variety of sources, including its own experts, whether medical or vehicular. The Highway Loss Data Institute (HLDI), a joint venture by several large auto casualty insurance companies, has very specific loss data by make and model of car.

Insurance companies have created claims problems by their ambiguous insurance policies and method of claims settlement.

The problems result from the vagueness of the terms chosen for the insurance contracts of reasonable charges for necessary repairs and not in excess of the regular and customary charges.

ASC takes the position that if insurance companies contract with their insureds and purposely use broad and vague terms in order to limit their liability, and then assume it is necessary to conspire with the provider industries to establish policy limitations, they cannot hide behind the McCarran-Ferguson shield. Such self created problems should not be shielded from review by granting special exemptions from FTC authority. ASC believes that insurers must include their terms of settlement in their policies. If they want limitations, they must clearly state their intention to restrict their liability at loss time to wage rates which are at the minimum or below the industry averages. They must provide in the contract that they will only reimburse policy holders for auto parts costs which are less than the cost of new parts. It is not essential to the industry to continue to control provider costs. However, where they believe controls are needed, such limits belong up front in clear terms in their contracts. Then insurance companies can compete with each other based on the stated limits of the losses they promise to pay their insureds—not some variable amount which may or may not reimburse the policy holder for the loss sustained.

When considering federal antitrust authority, it is essential that this committee understands the contractual relationship between third party suppliers (such as auto body repair shops) and the insureds. The vehicle owners, the insureds, are the customers of the body shops—not the insurance companies. The contract of repair is between the vehicle owner and the repair shops—not the insurance company. If the insurance company elects to repair under the policy, it then becomes the customer of the shop—but this is not the usual or customary practice.

Insurance companies are functionary parties which are simply returning to insureds portions of all premium dollars paid to them for the purpose of spreading the risks of losses. They have no legal basis for becoming the private regulators of the contracts between insureds and their suppliers. They have no basis for substituting their self interest, profit biased judgment for determining the terms and quality of performance by third party suppliers to their insureds. This self interest of the insurance companies creates a conflict of interest in the settlement procedure for their own insureds.

The insurance industry seeks to avoid all antitrust scrutiny and it has created several fictions. One fiction is that the public (the insureds) cannot be allowed to deal "one on one" with their providers. This has led the insurance companies to assume unto themselves the prerogative of determining what quality restoration is acceptable and at what price. Another fiction is that a little maximum price fixing and restraint of trade by groups of suppliers, induced by agreement or economic force of partially regulated insurers is good for the public. And, of course, the final fiction, described earlier, is that insurance companies are the large-scale purchasers of suppliers' services. Except in rare instances, the insured is the purchaser.

The first fiction has led to a public misperception that people are not totally responsible for their own acts concerning their health and property; that everyone and everything is insured against every loss; and that the insurance company is responsible and always pays. It is likely that this public misperception has increased insurance costs by encouraging unnecessary and exaggerated claims.

The second fiction is characterized by *Arizona* v. *Maricopa County Medical Society* (643 F2d 533 (9th Cir. 1980), cert. granted) now before the Supreme Court. It presents a situation where the evils of fee fixing by a provider body in agreement with the insurers, ultimately raises prices to a noncompetitive level, and adversely affects all purchasers or consumers of the providers' services, whether insureds or uninsureds.

The final fiction runs through many of the McCarran insurance-related cases where confusion exists about the point of purchase; who decides upon the type of service; who supplies and who receives the services and who is ultimately obligated to pay whom for all services.

ASC is concerned that the major, underlying issue before this committee has been obscured by the opponents to the FTC. The insurance industry mistakenly believes it must be protected against all antitrust actions in order to provide adequate public service. However, ASC members, as all providers, are concerned with restraints on their services, their earnings, and their freedom to serve the public. ASC believes that the major issue here is the proper balance, in the lawful positions of these related industries. Such balance will allow the interaction of adequate state regulation and federal antitrust laws to serve the true interests of the public.

In conclusion, ASC urges this committee to specifically direct the FTC to conduct an investigation of the casualty insurance companies' practices affecting consumers and to report to the Congress its findings together with any recommendations for legislation.

STATEMENT OF D. PAUL ALAGIA, JR.

I. PRELIMINARY STATEMENT

We are pleased to present this paper to the Committee and to address in a general manner the legal aspects of the Capper-Volstead Act, 7 U.S.C. Sections 291–292, and Section 20(a) of the Federal Trade Commission Improvements Act of 1980 [the "1980 Act"], which relate to agricultural cooperatives.

We are convinced that the Federal Trade Commission's recent conduct regarding agricultural cooperatives reflects the agency's failure to acknowledge the status accorded agricultural cooperatives under the antitrust laws by virtue of the Capper-Volstead and the 1980 Acts. Indeed, the current policies of the Commission concerning agricultural cooperatives misinterpret and flatly repudiate the clear and unquestionable intent of the Congress manifested in these enactments.

We respectfully suggest that steps must promptly be taken to prevent the Commission's continuing defiance of earlier-imposed Congressional prohibitions. Indeed, Section 22 of the 1980 Act itself confers on this Committee, through its Consumer Subcommittee, full responsibility to monitor and oversee Commission operations. Senator Kasten, the Chairman of the hearings on March 18 and 19, 1982 before the full Committee on Commission reauthorization and oversight, has reiterated not only an abiding commitment to "vigorous and effective oversight of the FTC" but also the need to "take stock of the Commission's activities periodically and to insure that the Commission is operating within its jurisdictional limits and in the interests of consumers." (Hearings on FTC Activities Concerning Professionals, U.S. Senate, 97th Cong., 1st Sess., Serial No. 97-59, July 15 and 17, 1981). We doubly welcome, therefore, the opportunity to present this Statement here.

For the reasons set forth in this paper, we advocate a clear and complete removal of FTC jurisdiction over agricultural cooperatives. Alternatively, we urge that such restrictions as already are or will be placed on the FTC's authority to study, investigate and prosecute agricultural cooperatives be set forth in language that is not susceptible to further distortion on the part of the Commission. Such statutory enactments are necessary because the Commission misperceives the statutory requirements of the 1980 Act to be nothing more than unenforceable admonitions, rather than the mandatory limitations on its authority which Congress intended.

Our support of Congressionally imposed restrictions on the Commission's authority vis-a-vis agricultural cooperatives stems from what we perceive to be conduct on the part of the Federal Trade Commission that violates the letter and spirit of the 1980 Act as well as the Capper-Volstead Act. More specifically, in our capacity as a counsel to Dairymen, Inc., a Capper-Volstead milk marketing cooperative, we have encountered significant abuses and excesses on the part of the Federal Trade Commission in connection with its investigation and prosecution of Dairymen.

By way of background, in September of 1978, the Commission initiated an investigation into Dairymen's 1978 acquisition of Farmbest Foods. That investigation culminated in the issuance of an administrative complaint in July of 1980, more than two months after passage of the 1980 FTC Improvements Act. Despite the express limitations imposed by the 1980 Act on Commission jurisdiction over agricultural cooperatives, the Commission complaint in no way seeks to justify its assertion of jurisdiction. Indeed, the complaint issued by the Commission makes no reference at all to the 1980 Act, the Capper-Volstead Act, or any conduct on the part of Dairymen which could be construed as predatory. Indeed, FTC complaint counsel have stated that they have no intention of showing predatory practices.

During the course of the protracted and expensive administrative proceeding, Commission staff have resisted all attempts of Dairymen's counsel to ascertain not only the substance of the required pre-complaint determination pursuant to the 1980 Act but also whether there was any administrative consideration and determination, as the law requires, that the challenged conduct—in this case the mere acquisition of Farmbest Foods—is not immunized under the Capper-Volstead Act. As discussed *infra*, in the landmark case of *Maryland & Virginia Milk Producers Association* v. *United States*, 362 U.S. 458, 471 (1980), the Supreme Court said that the mere acquisition of a proprietary by an agricultural cooperative "without more" is lawful under the Capper-Volstead Act.

A review of the record in the Dairymen case clearly demonstrates that the Commission has failed to discharge its statutory obligation under the Capper-Volstead Act and Federal Trade Commission Improvements Act of 1980. Again, the Commission clearly views the 1980 Act only as an admonition, not an express prohibition. By ignoring the express requirements of Section 20(a) of the 1980 Act, the Commission is attempting to nullify its basic purposes (i.e., protection of bona fide agricultural cooperatives like Dairymen from the staggering expenses of resonding to lengthy and costly FTC proceedings and prevention of the expenditure of FTC funds to prosecute agricultural cooperatives unless it is properly determined that the challenged activity is not immunized against antitrust liability).

The Commission's repeated refusal to acknowledge Dairymen's right to be free from prosecution under the 1980 Act, unless it has been properly determined that the challenged activity is not immunized under the Capper-Volstead Act, has had the effect of obliterating a right accorded agricultural cooperatives and guaranteed by the express language of Section 20(a) of the 1980 Act.

We further maintain that the Commission has misperceived the entire purpose of the 1980 Act's express limitations on Commission jurisdiction over agricultural cooperatives vis-a-vis the role of the Secretary of Agriculture. The Commission's conduct has ignored the Congressional insistence, reiterated in the 1980 Act's legislative history, that the Commission seek and obtain from the Agriculture Department a ruling that the cooperative conduct it seeks to challenge is not entitled to Capper-Volstead immunity.

The Commission's failure to observe the jurisdictional limitations of Section 20(a) of the 1980 Act constitute clear and compelling justification for Congress to enact legislation expressly limiting the Commission's jurisdiction vis-a-vis agricultural cooperatives.

II. THE CAPPER-VOLSTEAD ACT AND THE FEDERAL TRADE COMMISSION ACT OF 1980

Section 20 of the 1980 Act, is entitled "Restriction of Commission Authority Relating to Agricultural Cooperatives." It provides in pertinent part:

"The Federal Trade Commission shall not have any authority to use any funds which are authorized to be appropriated to carry out the Federal Trade Commission Act for fiscal year 1980, 1981, or 1982 . . . for the purpose of conducting any study, investigation, or prosecution of any agricultural cooperative for any conduct which, because of the provisions of the . . . Capper-Volstead Act, is not a violation of any Federal antitrust act or the Federal Trade Commission Act." [1]

Congress passed Section 20(a) of the 1980 Act specifically for the protection of Capper-Volstead agricultural cooperatives. The language, purposes and history of the 1980 Act demonstrate that the FTC cannot simply presume that conduct by an agricultural cooperative is not exempt by reason of the Capper-Volstead Act from its scrutiny.

In this paper we focus primarily on the processing functions of marketing agricultural activities for two reasons: (1) marketing agricultural cooperatives are for sound business reasons increasingly become processors of their members' raw products; and (2) the FTC is more likely to challenge the activities by associations of farmers, claiming they are not protected by Capper-Volstead, when farmers' activities involve expansion of their processing capabilities by external means.

A. Background of the enactment of section 20

The Conference Committee which finalized the 1980 Act stated: "This section has been added to ratify the spirit and intent of the Capper-Volstead Act. The Conferees believe that the rationale for the limited antitrust exemption contained in the statute is valid." Rep. No. 96-917, 96th Cong., 2d Sess. 37 (1980).

In addition to reviewing the purposes and intentions of Congress in adopting Section 20(a), we briefly discuss in this paper the "spirit and intent" of the Capper-Volstead Act. Senator Ford, a Conferee on the bill, explained Section 20 as follows: "This amendment addresses the uncertainty surrounding the jurisdiction of the FTC by making certain that the FTC may not take any action against agricultural cooperatives because of conduct that is exempt from antitrust enforcement under the Capper-Volstead Act. This amendment says that if the Capper-Volstead Act sanctions certain activities, the FTC has to stay away—totally. It may not initiate any action whatsoever." Attachment 1 at 26.

It was the House of Representatives that first considered and passed provision relating to agricultural cooperatives. On November 27, 1979, Senator (then Congressman) Andrews proposed an amendment to H.R. 2313 to restrict the FTC's authority relating to agricultural cooperatives. 125 Cong. Rec. H11189 (daily ed. 1979). This amendment provided:

RESTRICTION OF COMMISSION STUDIES AND INVESTIGATIONS RELATING TO AGRICULTURAL COOPERATIVES

SEC. 305. The Federal Trade Commission shall not have any authority to use any funds which are authorized to be appropriated to carry out the Federal Trade Commission Act (15 U.S.C. 41 et seq.) for fiscal year 1980, 1981, or 1982, for the purpose of—

(1) conducting any study, investigation or prosecution of any agricultural cooperative which meets the requirements of the Act entitled "An Act to authorize association of producers of agricultural products", approved February 18, 1922 (7 U.S.C. 291-292), commonly known as the Capper-Volstead Act; or

(2) conducting any study or investigation of any agricultural marketing orders.

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[1] In Attachment 1 to this paper, we provide the complete text of Section 20 and highlight the abundant legislative history materials fully confirming the correctness of the points we make here. [Attachment 1 to this paper has been retained in Senate Commerce Committe files.]

Representative Glickman proposed that the following language be added to the Andrews amendment: "except that the Commission shall have authority to undertake any such action with respect to false and misleading advertising." 126 Cong. Rec. H 11189. The amendment was approved and this conditional language was added after the words "the Capper-Volstead Act" in the Andrews amendment.

After a brief but informative debate (125 Cong. Rec. H 11189–H 11202) the Andrews amendment was passed on November 27 by a vote of 245 to 139. 125 Cong. Rec. 11201. H.R. 2313 was passed as amended by the House on the same day. 125 Cong. Rec. H 11206.

The Senate considered S. 1991 in the second session of the 96th Congress on February 7, 1980. 126 Cong. Rec. S 1177–S 1242 (1980). The Senate passed H.R. 2313 in lieu of the Senate bills S. 1020 and S. 1991 (126 Cong. Rec. S 1242) after amending its language to contain much of the text of the Senate bills. However, the Andrews amendment was not included in the Senate's version of the H.R. 2313.

In the conference on H.R. 2313, the Conference Committee amended the language of the Andrews amendment and the new version became Section 20(a) of the Act. According to Representative Scheuer, a Conferee, "the conference substitute maintained the intent of the House amendment" with respect to agricultural cooperatives. 126 Cong. Rec. H 3858. Thus, the final version of Section 20(a) was, in substance, the same as the Andrews amendment which passed the House, albeit the language was slightly different. Reference to the Congressional explanation of Section 20(a) (then Section 305) when it passed the House is entirely appropriate.

When Senator Andrews introduced his amendment to the 1980 Act, which subsequently became, in amended form, Section 20 of the 1980 Act, the phrase "which meets the *requirements* of the Act" in paragraph (1) of the amendment (Attachment 1 at p. 7) did not merely distinguish between Capper-Volstead associations of producers and non-Capper-Volstead associations. The "requirements" of the Capper-Volstead Act include several conditions that must be met before the protections which is provides can be obtained. The protected persons must be engaged in the production of agricultural products and they must be acting collectively in processing, in preparing for market, handling, and marketing their products for the *mutual* benefit of the members. Senator Andrews and the House, which overwhelmingly passed his amendment, were fully cognizant of both the requirements of the Capper-Volstead Act and the specific types of conduct it exempted from the antitrust laws.

After the 1980 Act (and the Andrews amendment) initially passed the House and the Senate, the Conference Committee slightly changed the language of the Andrews amendment. Instead of the phrase "which meets the requirements of the Act," the Conference Committee added the phrase "for any conduct which, because of the provisions of the [Capper-Volstead] Act . . . is not a violation of any Federal antitrust act or the Federal Trade Commission Act." (Attachment 1 at p. 1). In view of the fact that the Andrews amendment had also covered the conduct of agricultural associations, the change in the language by the Conference Committee was merely formal and clarifying in nature and not substantive. Because Congress desired to continue the Capper-Volstead Act's and Clayton Act's Section 6 protection of the cooperative activities of farmers, the Committee's clarification of the language was understandable.

The Conference Committee's report on the 1980 Act clearly demonstrated Congress' intent to confirm fully the exemptions of the Capper-Volstead Act. The language of the Conference Committee report quoted above shows that the conferees did not intend in any manner to detract from the rationale underlying the Andrews amendment which the House had voted 245–139 to approve. 125 Cong. Rec. H 11201.

Therefore, because both the original Andrews amendment and the final version of it which came out of conference were directed at the authority of the FTC to investigate, study and prosecute the *activities* of Capper-Volstead agricultural associations, the legislative history which accompanied the Andrews amendment in the House is entirely relevant in understanding Section 20 as finally enacted by Congress.

B. Purposes of Section 20(a)

1. Restrictions on FTC jurisdiction.—The purpose of Section 20 of the 1980 Act was best expressed by Senator Ford when he said that "the FTC has to stay away—totally" from the antitrust prosecution of Capper-Volstead cooperatives. Those Congressmen who favored the Andrews amendment applauded the proposal to restrict the FTC from engaging in regulatory functions which were not within its proper sphere. *See, e.g.,* Attachment 1 at 4–5, 8, 9, 10 (remarks of Rep. Andrews); 5–6 (remarks of Rep. Wampler); 6–7 (remarks of Rep. Abdnor); 7 (remarks of Rep. Roth); 7, 8 (remarks of Rep. Grassley); 9 (remarks of Rep. Coelho); 12 (remarks of Rep. Pashayan); and 13 (remarks of Rep. Sebelius). Opposition to the Andrews amendment stemmed from objections to so limiting FTC jurisdiction over farmer cooperatives. *See* Attachment 1 at 22 (remarks of Rep. Eckhardt).

The intent to keep the FTC "totally" away from scrutinizing the conduct of agricultural cooperatives was demonstrated by the overwhelming congressional insistence on retention of exclusive regulatory power in the hands of the Secretary of Agriculture. For example, Representative Abdnor noted that:

"[Q]uite clearly [the] statutory authority for the regulation of agricultural cooperatives rests with the Secretary of Agriculture, pursuant to the provisions of the Capper-Volstead Act. Unfortunately, the Federal Trade Commission has seen fit to preempt this authority and initiate its own investigation into agricultural cooperatives' activities." [Attachment 1 at 7.]

"[i]t behooves us to adopt the [Andrews] amendment and prevent this kind of duplication. Congress has stated its intent that agricultural cooperatives grow and prosper. Therefore it is imperative that we correct a serious situation which has resulted in cooperatives incurring significant expenses in dealing with the investigative whims of the FTC." [Attachment 1 at 19.]

"Again, I . . . urge my colleagues to support our efforts to prohibit the Federal Trade Commission from continuing its investigations into agricultural cooperatives." [Attachment 1 at 7.]

Representative Grassley, in supporting the Andrews amendment, observed that "this amendment is designed to eliminate any controversy over which agency has the antitrust responsibility for agricultural cooperatives. The Department of Agriculture is the agency best suited to do this." Attachment 1 at 8. The House view that the FTC should not have jurisidiction over Capper-Volstead cooperatives prevailed in the 1980 Act. The debate in Congress makes it clear that this view followed the goals set by Congress in the passage of the Capper-Volstead Act of 1922. Those goals are illustrated by the following brief review of the legislative history of the Capper-Volstead Act.

In 1919, Congress began efforts to strengthen the protection afforded agricultural cooperatives by Section 6 of the Clayton Act. The legislative history of the Capper-Volstead Act reflects a sharp debate over whether the FTC or the Department of Agriculture should have antitrust jurisdiction over the activities of agricultural cooperatives. The debate continued for three years with the House Committee on Agriculture seeking to confer jurisdiction on the Secretary of Agriculture while the Senate Judiciary Committee favored the FTC.

When the House Judiciary Committee reported on H.R. 2373 (which became Capper-Volstead), the Report contained the following paragraphs which had not previously been contained in reports on the agricultural cooperative bill. These paragraphs related to a proposed section 2 of the bill (7 U.S.C. § 292):

"This bill directs the Secretary of Agriculture to supervise these associations. The reason for that is apparent when one considers the duties and the organization of that department. The Secretary has for many years aided farmers in forming such associations, and his department is thoroughly familiar with the needs and the difficulties under which they always have to struggle. There is in his department a Bureau of Markets that is constantly engaged in studying marketing conditions and prices of agricultural products both in this and foreign countries. As a consequence, he is especially well equipped for the purpose of determining whether the prices charged by any of these associations are excessive. That is one of the duties that somebody must perform to safeguard the public.

"If it is safe not to place a limit upon the size of an ordinary corporation, there certainly is no reason to fear monopoly from farm associations. But in the event that any such association should monopolize or restrain trade so as to unduly enhance the price of an agricultural product, ample provision is made in the bill to protect the public. The Secretary of Agriculture, in a sundry fashion, can grant relief, and he, with his expert knowledge always at hand, can act more expeditiously than could any other agency. In the event an association fails to abide by his judgment, it can not only be hauled into court, but a temporary injunction can at once be issued against it."

H.R. Rep. No. 24, 67th Cong., 2d Sess. 3 (1921). Thus, the House intended that the Secretary of Agriculture scrutinize agricultural cooperatives for possible antitrust violations.

On the other hand, the Senate Judiciary Committee, upon referral of H.R. 2373 (61 Cong. Rec. 1058 (1921)), proposed to add the following amendment to the bill:

"Nothing herein contained shall be deemed to authorize the creation of, or attempt to create, a monopoly, or to exempt any association organized hereunder from any proceedings instituted under the Act entitled "An Act to Create a Federal Trade Commission, to Define its Powers and Duties, and For Other Purposes," approved September 26, 1914, on account of unfair methods of competition in commerce."

S. Rep. No. 236, 67th Cong., 1st Sess. 1 (1921). This amendment purported to subject agricultural cooperatives to FTC Jurisdiction. Senator Walsh, the author of the amendment, noted that the amendment was intended to resolve the question of whether or not regulatory authority would repose with the FTC. Hearings on H.R. 2373 before the Senate Comm. on the Judiciary, 67th Cong., 1st Sess. 15 (1921).

In an attempt to persuade the Senate to pass the House version of the bill without the Senate Judiciary Committee anti-monopoly amendment, Senator Kellogg observed:

"The Attorney General has the duty placed upon him to take charge of the suit in the Court and to prosecute it, but the Attorney General has not the machinery to study these cooperative associations, to find out the cost of production, the cost of selling, the reasonable prices to consumers, and various other elements which it is easy for the Secretary of Agriculture to find out.

"It may be said, therefore, that before such associations can be prosecuted under the Sherman Act, for any restraint of trade or monopoly, whether it is a mere technical monopoly or not, the Secretary of Agriculture must investigate and make a finding that the cooperative association is in restraint of trade or is a monopoly and is unduly enhancing prices."

62 Cong. Rec. 1978, 2048 (1922). Such comments, in contrast to dissenting views favoring FTC jurisdiction over agricultural cooperatives, show that an "either-or" decision had to be made by Congress. See, e.g., 62 Cong. Rec. 2278–79 (1922) (remarks of Sens. Norris and King).

Following this discussion, an amendment was offered substituting the words "Federal Trade Commission" for the words "Secretary of Agriculture" wherever they appeared in the House version. Confronted directly with the responsibility of selecting between the two administrative agencies, the Senate rejected this proposed amendment, thus flatly rejecting FTC jurisdiction over Capper-Volstead cooperatives. Furthermore, the Senate Judiciary Committee's anti-monopoly amendment was soundly defeated. 62 Cong. Rec. 2281 (1922). The Congress then approved the House version and H.R. 2373 was enacted into law as the Capper-Volstead Act.

The legislative history of the Capper-Volstead Act further establishes that Congress rejected FTC jurisdiction because of a sincere distrust of the Commission's fact-finding ability with regard to agricultural cooperatives. *See, e.g.,* 60 Cong. Rec. 366–67 (1920) (remarks of Senator Lenroot on the Capper-Volstead predecessor bill, H.R. 13931); 59 Cong. Rec. 8035 (1920) (remarks of Rep. Browne); and Hearings on H.R. 7783 Before the House Committee on the Judiciary, 66th Cong., 1st Sess. 20 (1919) (statement by John Miller). Moreover, the comments of the Senate floor manager and the language of the House Report on the Capper-Volstead Act show a strong preference for the fact-finding abilities of the Secretary of Agriculture. 62 Cong. Rec. 2049 (1922); H.R. Rep. No. 24, 67 Cong., 1st Sess. 3 (1921).

The legislative history of the Capper-Volstead Act and the language and structure of the Act establish that at least at the administration level[2] only the Secretary of Agriculture, and not the FTC, may exercise jurisdiction over agricultural cooperatives.

A simple review of the language of the Capper-Volstead Act and the language of Section 7 of the Clayton Act illustrates the unnecessary duplication of antitrust regulation over important conduct of agricultural cooperatives relating to marketing. Under the Capper-Volstead Act, 7 U.S.C. § 292, the Secretary of Agriculture "shall serve upon such association a complaint" if he: "shall have reason to believe that any such association monopolizes or restrains trade in interstate or foreign commerce to such an extent that the price of any agricultural product is unduly enhanced by reason thereof."

Under 7 U.S.C. §292, the Secretary can then issue an order directing the association to cease and desist from monopolization or restraint of trade.

The FTC, on the other hand, issues complaints against unfair methods of competition based upon a reason to believe standard pursuant to 15 U.S.C. § 45(b). The

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[2] Those cases which hold that the jurisdiction of the Secretary of Agriculture is not "exclusive" and that, therefore, an agricultural cooperative is subject to judicial suit by the United States Justice Department, do not address the questions of FTC jurisdiction discussed above and do not rebut the conclusion that the FTC does not have jurisdiction over agricultural cooperatives. *See, United States* v. *Borden Co.,* 308 U.S. 188 (1939); *Maryland & Virginia Milk Producers Association, Inc.* v. *United States,* 362 U.S. 458 (1960). We recognize that the Secretary of Agriculture does not have jurisdiction over Capper-Volstead cooperatives to the exclusion of the Attorney General.

FTC's jurisdiction generally reaches conduct prohibited under the provisions of the Clayton Act, specifically Section 7 of that Act (15 U.S.C. § 18), which declares certain acquisitions to be unlawful. The acquisitions prohibited are those which may substantially lessen competition, or which may tend to create a monopoly.

A marketing agricultural cooperative which acquires necessary processing facilities from a non-cooperative party is, therefore, faced with two regulatory bodies and its conduct scrutinized under two similar statutes. The Capper-Volstead Act includes the words "restrains trade" while Clayton Act Section 7 says "may substantially lessen competition." In addition, Capper-Volstead contains the word "monopolizes," while Clayton Section 7 says "may tend to create a monopoly." Congress should make it clear that as to cooperative acquisitions such overlapping regulatory authority does not apply.

2. Remove from agricultural cooperatives the burden of costly and disruptive administrative proceedings.—Congress in the 1980 Act intended that agricultural cooperatives be shielded from the costs of burdensome FTC proceedings grounded on conduct exempted by the Capper-Volstead Act. This is abundantly clear from the legislative history.

Senator Andrews stated: "It is deplorable for me to think that farmer money must be used to defend against Government intervention. I want to do everything I can to guard against this continuing high cost to farmers and their cooperatives. They have a much more important task than to spend their time and money fighting the FTC. They have a nation and much of the world to feed."

Attachment 1 and 19. Representatives Abdnor, Coelho, and Johnson expressed the same views. Attachment 1 and 19, 20 and 21, respectively. Representative Coelho noted that the legal fees and direct expenses forced by FTC on agricultural cooperatives run into the millions of dollars. He said cooperatives cannot, unlike corporate giants, endure the fight against FTC for long because they lack the resources to finance it. Attachment 1 at 20. Representative Johnson called the impact on a farmers' cooperative "vast, cruel and punishing." Attachment 1 at 21.

This clearly articulated and explicit purpose of the 1980 Act brings into even sharper focus the illegal nature of the FTC's continuing prosecution of agricultural cooperatives.

C. The practical effect of section 20(a) on the acquisition of processing facilities

The basic question which Congress in Section 20(a) required to be asked is: Would the FTC have jurisdiction over an agricultural cooperative for conduct which does not violate the antitrust laws? We will review this issue in light of Congress' intention expressed in 1921 and in 1980 that processing was a legitimate and protected activity of a marketing agricultural cooperative.

The Capper-Volstead Act expressly includes "processing" as one of the immunized activities engaged in collectively by farmers. 7 U.S.C. Section 291. The following colloquy between Senators DeConcini and Ford, during consideration of the bill which became the 1980 Act, confirms that the Capper-Volstead exemption includes contracts and agreements entered into by a cooperative in connection with processing:

Mr. Ford. * * * Simply put the Commission has no business tampering with cooperative activities that fall within the Capper-Volstead Act.

Mr. DeConcini. Am I correct, that the conferees agree that the antitrust exemption in the Capper-Volstead Act includes contracts and agreements entered by a cooperative in connection with the processing, preparing, handling, and marketing of agricultural products?

Mr. Ford. My distinguished colleague from Arizona is correct. While we are reluctant to describe definitely the scope of the exemption with respect to all issues, it is clear that for Capper-Volstead to have any meaning, a cooperative must have the freedom to enter contracts and agreements to further the "legitimate" interests of its members.

126 Cong. Rec S 5689 (daily ed. May 21, 1980) (Attachment 1 at 27). In their view, the word "processing" only has meaning if a cooperative consisting of dairy farmers has the freedom to enter into contracts and agreements (e.g., the acquisition of processing facilities) necessary to further the particular legitimate interest of processing the milk of its members.

The following colloquy further demonstrates that the thrust of the House amendment was to restrict FTC's authority to investigate most acquisitions by farmers of processing facilities owned by non-farmers:

Mr. Eckhardt. What about a merger of a co-op with a non-co-op, particularly a case against a non-co-op partner?

Mr. Andrews of North Dakota. I would assume the FTC would not have the jurisdiction. The jurisdiction would lie with the Department of Agriculture.

Mr. **Eckhardt**. The gentleman does not intend to change the law if the FTC does have the jurisdiction to attack such a merger as a creation of monopolization? This amendment does not change it?

Mr. **Andrews** of North Dakota. If the FTC action would be to limit the ability of a co-op to grow, the thrust of my amendment would be to limit that FTC ability to clamp down on the agricultural cooperative. Congress intended agricultural cooperatives to have the ability to band together and become in a sense types of monopolies in their field so they could get better prices for their small products.

125 Cong. Rec. H 11193 (daily ed. Nov. 27, 1979) (Attachment 1 at 11).

These views only confirm the type of conduct of agricultural cooperatives which Congress in 1921 exempted from antitrust scrutiny. The legislative history of the Capper-Volstead Act makes clear that Congress desired that farmers through voluntary cooperation not only bargain as equals with large corporate buyers, but to some extent replace them as "middlemen" in the marketing of farm goods. H.R. Rep. No. 24, 67th Cong., 1st Sess. 3 (1921) (61 Cong. Rec. 687); 61 Cong. Rec. 1033, 1035, 1040 (1921); 62 Cong. Rec. 2060, 2159, 2216, 2218, 2257, 2264 (1922). The House Report accompanying the Capper-Volstead Act pointed out that existing associations had been able to replace many of the middlemen that stood between the producers, the retailers, and the consumers. Such middlemen, the Report stated, were one of the chief problems these associations had in getting their products to the consumer with as little expense as possible. The Report concluded that, "[f]armers ought to be given a chance to do that." H.R. Rep. at 3. Among the "middlemen" which concerned Congress were the processors which agricultural cooperatives must face in the marketplace.

The Supreme Court decided the landmark case of *Maryland and Virginia Milk Producers Association* v. *United States*, 362 U.S. 458 (1960), more than 20 years before Congress passed the 1980 Act. The Court in *Maryland & Virginia* stated, based upon its reading of the legislative history, that the Capper-Volstead Act "did not leave cooperatives free to engage in practices against other persons in order to monopolize trade, or restrain and suppress competition with the cooperative." 362 U.S. at 467. (Emphasis added.) The Court's inclusion of the emphasized words was not inadvertent. It could have simply left the emphasized words out without losing antitrust significance. But for a cooperative, the kind of practices against others was most significant.

Predation was at the heart of *Maryland and Virginia*. As the Court noted, the defendant's purpose was to "eliminate the Association's prime competitive dealer from government contract milk bidding; and increase the Association's control of the Washington market." *Id.* at 469. The reason for eliminating the competitor was that its "competitive practices . . . had made Embassy a 'thorn in the side of the Association for many years.' " Id. at 470. In discussing the inapplicability of the exemption to the defendant's actions, the Court referred to them as "competition-stifling practices" and "predatory practices," Id. at 463, "predatory trade practices," id at 466, and as designed "to achieve monopoly by preying upon independent producers," id. at 467. It was on this basis that the Court was "satisfied that the allegations of the complaint and the statement of particulars . . . charge anticompetitive activities which are so far outside the 'legitimate objects' of a cooperative that, if proved, they would constitute clear violations of Section 2 of the Sherman Act . . .". Id at 468. It was these practices also that illegally tainted the Association's permissible processing and marketing business and transformed the acquisition of a proprietary's assets from a possible necessary contract (santioned explicitly by Capper-Volstead) into an unlawful restraint of trade. Id. at 471–72.

The acquisition in *Maryland & Virginia* was, according to the Supreme Court, not made merely to advance the Association's permissible marketing objectives but rather as as weapon to restrain and suppress competition, therefore violating Section 7 of the Clayton Act as well as Section 3 of the Sherman Act. 362 U.S. at 369, 471–72.[3] However, the Court recognized that because of the legitimate purposes processing facilities may serve, it assumed that their purchase by a cooperative for business use would "without more" be permitted and would be lawful under Capper-Volstead. Id. at 471. Such purchase would be lawful notwithstanding either the Clayton or Sherman Acts. The admonition against predatory practices (and conversely the Capper-Volstead exemption) applies to all sections of the antitrust laws. The Court in *Maryland & Virginia* expressly recognized that the Capper-Volstead exemption does not lend itself to "incongruous immunity-distinction between the sections" of the antitrust laws. Id. at 464.

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[3] Consistent with the Supreme Court's decision in *Maryland & Virginia*, Representative Broyhill stated during the House's consideration of the Conference Report to the 1980 Act that "an agricultural cooperative may grow with respect to numbers of members and market shares to any size which it can obtain as long as it does not engage predatory practices in order to attract and keep members or obtain a larger market share." 126 Cong. Rec. H 3859–H 3860 (daily ed. May 20, 1980).

When the 1980 Act was passed, the Capper-Volstead exemption already extended to contracts and agreements between farmer cooperatives and non-cooperative organizations which facilitate the legitimate interest of farmers, including a non-predatory contract or agreement between farmers and other to acquire processing facilities in furtherance of the cooperative's legitimate marketing functions.[4]

Since enactment of the 1980 Act, the Second Circuit and two district courts have held that a showing of predatory conduct is essential to override a claim that, certain conduct by an agricultural cooperative, or cooperative acting in concert, is exempt sections 1 and 2 of the Sherman Act.

The Court of Appeals for the Second Circuit, relying upon *Maryland & Virginia*, held that Section 2 of the Sherman Act "does not apply to monoply power that results from such acts as the formation, growth and combination of agricultural cooperatives, but applies only to the acquisition of such power by other, predatory means." *Fairdale Farms, Inc.* v. *Yankee Milk, Inc.*, 635 F. 2d 1037, 1045 (1980), cert. denied, — U.S. —, 70 L. Ed. 2d 88 (1981). Moreover, the Second Circuit emphasized that unless "predatory acts had been sufficiently shown," the agricultural cooperative's motion for summary judgment with respect to the Sherman Act Section 2 claim should be granted. *Id.* The Second Circuit's holding on predation was the pivotal issue raised in *Fairdale Farms'* petition for certiorari. The Supreme Court denied certiorari and thus left intact the Second Circuit's holding.

At the core of the Second Circuit's decision are the two essential elements of a Sherman Act Section 2 monopolization claim against an ordinary business corporation. The first is the possession of monopoly power in the relevant market. The second is the willful acquisition or maintenenace of that power. The district judge in *Fairdale Farms* applied the ordinary corporate monopolization test which "proscribes the willful acquisition of monopoly power that is not the result of 'a superior product, business acumen, or historic accident'." Id. at 1040, 1044–45. This was error, held the Court of Appeals, because such application of the corporate monopolization test misconstrued the Congressional intent evidenced in the Capper-Volstead Act. Id. at 1040. The court, after carefully reviewing the Capper-Volstead exemption, concluded that the second element, namely the willful acquisition or maintenance of monopoly power, "is exactly what Capper-Volstead permits." Id. at 1045.

Having recognized that the willful acquisition or maintenance of monopoly power by an agricultural cooperative—either alone or in combination with other cooperatives—is a perfectly lawful pursuit, the court, of necessity, added a third element. That element is that the willful acquisition or maintenance of monopoly power be by "predatory means." Id.

The Second Circuit's extensive review of the Capper-Vostead exemption, its legislative history, other pertinent statutes, and court decisions led it to observe that:

"The consistent tenor of the enactments shows that Congress wanted and expected farmers to be represented by strong and effective cooperatives, so extensively organized as to be representative of individual commodities. [635 F. 2d at 1043]

* * * * * * *

"[N]o association can efficiently operate that does not control and handle a substantial part of a given commodity in the locality where it operates." [Id., quoting 62 Cong. Rec. 2058 (1922) (S. Rep. No. 256)]

"As the cooperative grows, so, normally, does its power over the market. Thus while the formation, growth and operation of a powerful cooperative is obviously a 'willful acquisition or maintenance of such power,' and will rarely result from 'a superior product, business acumen, or historic accident,' it is exactly what Capper-Volstead permits. [Id. at 2045]

* * * * * * *

"It is not a violation of the Sherman Act for the members of an agricultural cooperative to carry out the legitimate objects of their association which follow naturally from their attempts to achieve unity of effort and the voluntary elimination of competition among themseleves. [Id.]"

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[4] The agreement with "outsiders" found to be unprotected by the Capper-Volstead exemption in *United States* v. *Borden*, 308 U.S. 188 (1939), was a widespread conspiracy involving, among others, municipal officials and a union. In *National Broiler Marketing Association* v. *United States*, 436 U.S. 816 (1978) and in *Case-Swayne Co.* v. *Sunkist Growers, Inc.*, 389 U.S. 384 (1967), non-farmers were members of the associations opening up the associations' activities to antitrust scrutiny.

The Second Circuit warned, however, that a cooperative can neither acquire nor exercise monoply power in a predatory fashion by the use of such tactics as picketing and harrassment, boycotts, coerced membership and discriminatory pricing. Id. at 1044 (citations omitted). Nor could a cooperative use its legitimately acquired monopoly power in such a manner as to stifle or smother competition, as described in *Maryland & Virginia* and in *Berky Photo, Inc.* v. *Eastman Kodak Co.* 603 F. 2d 263, 274 (2d Cir. 1979), cert. denied, 444 U.S. 1093 (1980).

Following *Fairdale Farms,* the district court in *Kinnett Dairies, Inc.* v. *Dairymen, Inc.,* 512 F. Supp. 608 (M.D. Ga. 1981), held that Dairymen's activities, viewed either with or without Capper-Volstead's protection, did not violate either Section 1 or Section 2 of the Sherman Act. Section 1 was not violated because Capper-Volstead grants full immunity to Capper-Volstead organizations acting separately or collectively in fixing prices and in conducting other marketing activities, absent agreements with outsiders. Section 2 was not violated because Capper-Volstead grants full immunity to such violations, absent agreements with outsiders and absent predatory conduct in violation of the Sherman Act. 512 F. Supp. at 643. The Court found conspiciously absent the predatory tactics enumerated in *Fairdale Farms. Id.* at 642. The Capper-Volstead exemption protected Dairymen's "unilateral" activities, i.e., those directed at its customer (and competitor) handlers because the court found "predation eliminated largely by admission, and entirely by evidence and the lack thereof, and . . . no conscious intent to stifle or smother competition or to exclude others from the market place." Id. at 643.

In another district court decision to follow the lead in *Fairdale, GVF Cannery, Inc.* v. *California Tomato Growers Association, Inc.,* 1981-1 Trade Cases ¶64,088 (N.D. Cal. 1981), the district court stated that it would grant judgment to the defendant agricultural cooperatives for the claims alleged under Section 2 of the Sherman Act unless plaintiff could demonstrate in an amended complaint that the cooperatives engaged in predatory conduct. On the subsequent complaint, the court ruled that the three specific acts alleged could not, under the case law, be characterized as predatory, and granted jugement. *GVF Cannery, Inc.* v. *California Tomato Growers Association, Inc.,* 1981-2 Trade Cases ¶64,200 (N.D. Cal. 1981). The Supreme Court of the State of Washington recently relied upon these and other cooperative cases in holding that the cooperative was not liable for damages on an antitrust claim. *Consolidated Dairy Products Co.* v. *Bar-T Ranch Dairy, Inc.*

One case, *United States* v. *Dairymen, Inc.,* 660 F.2d 192 (6th Cir. 1981), conflicts with *Fairdale Farms,* the other cases discussed above and, we believe, the statutes and the legislative history embodying the Capper-Volstead exemption. The Sixth Circuit would treat Dairymen as an ordinary business corporation in determining whether it unlawfully attempted to monopolize.

Fairdale Farms, Kinnett v. *Dairymen,* and the legislative history accompanying the Capper-Volstead Act establish that agricultural cooperatives may willfully obtain a monopoly. Even the Sixth Circuit recognized this. *Maryland & Virginia, Fairdale Farms, Kinnett* v. *Dairymen, GVF Cannery* and the Capper-Volstead legislative history also unanimously confirm that agricultural cooperatives may exercise monopoly power in pursuit of legitimate marketing objectives, the core of which is obtaining and maintaining equal bargaining position vis-a-vis those with whom they must deal in the marketplace.

We believe that, just as the court in *Fairdale Farms* held the ordinary Section 2 standard in a monopolization case does not apply to monopoly power of agricultural cooperatives resulting from non-predatory means, so too the complete standard applied to ordinary business corporations in a attempt-to-monopolize case does not apply to an agricultural cooperative's conduct. This is because two of the three elements of that standard, i.e., specific intent to monopolize and dangerous probability of success, are greatly affected by the Capper-Volstead exemption.

Applying *Maryland & Virginia, Fairdale Farms, Kinnett* v. *Dairymen* and *GVF Cannery* to a Clayton Act Section 7 case brought by the FTC against an agricultural cooperative, we believe that the standard applied to ordinary business corporations for violations of that section cannot apply. If a cooperative or a group of cooperatives acting in concert can willfully set out to obtain and maintain monopoly power by non-predatory means, certainly the acquisition of non-cooperative assets in a non-predatory fashion cannot unlawfully "tend to create a monopoly." With respect to the second element of a Section 7 case (i.e., "the effect of such acquisition may be substantially to lessen competition"), in the absence of predation, the purposes and effects (real or potential) of an acquisition of processing facilities cannot legally be compared to the acquisition present in *Maryland & Virginia.* In any event, the Secretary of Agriculture pursuant to the Capper-Volstead Act (7 U.S.C. § 292) could scrutinize the acquisition even if it only "restrains trade."

Because Congress both in the Capper-Volstead Act and in the 1980 Act, and the Supreme Court in *Maryland & Virginia,* viewed the acquisition of processing facilities as a legitimate function and objective of an agricultural market cooperative, a tension necessarily arises between the exemption and the "substantially lessening competition" language of Section 7. Congress gave agricultural associations the green light to build, acquire and ultimately maintain facilities in which to process the products of its producers. The Capper-Volstead exemption does not stop protecting this legitimate function when the ownership of processing facilities is realized by way of an acquisition from a non-cooperative, which acquisition also may tend to lessen competition. If it did, then the word "processing" in the Capper-Volstead Act becomes hollow and the intent of Congress to equalize the bargaining position of cooperatives in the marketplace would be nullified. Congress did not perceive the Capper-Volstead exemption in such a fashion.

CONCLUSION

We have attached hereto two legislative proposals amending Section 20 of the 1980 Act, 15 U.S.C. § 57c (note) (Attachments 2 and 3). If adopted, either of these proposals would help ensure against further abuses by the Commission of its authority.

The first was submitted to this Committee by the National Council of Farmer Cooperatives. We fully support the concept addressed by its suggested amendments. However, in the second proposal attached, we offer several slight revisions to those suggested amendments.

Agricultural marketing associations can, and often must, become processors as well. Congress' ultimate purpose was to make agricultural associations competitive in the marketplace. A marketing agricultural cooperative often faces customers who are large conglomerates. Because some cooperatives also happen to be processors, such large conglomerates are also the cooperative's competitors in the sale of fluid milk and cultured products.

It is important for a cooperative to be able to process the milk produced by its members. It serves the legitimate purpose of assuring outlets for its members' milk. Moreover, it permits an agricultural cooperative to deal with conglomerate, nonfarmer processors on a more equitable basis. This is what Congress wanted to achieve in the Capper-Volstead Act.

The Federal Trade Commission's attempted application of Section 7 of the Clayton Act to a legitimate, non-predatory acquisition of clearly useful proprietary processing facilities by an agricultural cooperative negates the Congressional purpose and further ignores the fact that the relevant legislative enactments—the Capper-Volstead Act and the 1980 Act—constitute a substantial part of what one United States Court of Appeals recently described as a Congressional policy treating agricultural cooperatives as a "favorite child." *Fairdale Farms, Inc.* v. *Yankee Milk, Inc.,* 335 F.2d 1037, 1043 (2d Cir. 1980), *cert. denied,* — U.S. —, 70 L.Ed.2d 88 (1981).

[ATTACHMENT 2]

RESTRICTIONS OF COMMISSION STUDIES AND INVESTIGATIONS RELATING TO AGRICULTURAL COOPERATIVES

Section 5(a) of the Federal Trade Commission Act (15 U.S.C. 45a) is amended by adding at the end thereof the following new paragraph.

Section 305(a). The Federal Trade Commission shall not have any authority to use any funds which are authorized to be appropriated to carry out the Federal Trade Commission Act (15 U.S.C. 41 et seq.) for the purpose of

(1) conducting any study or investigation of any agricultural marketing orders,

(2) conducting any study, investigation, or prosecution of any agricultural cooperative which meets the requirements of the Act entitled "An Act to authorize association of producers of agricultural products" approved February 18, 1922 (7 U.S.C. 291-292), commonly known as the Capper-Volstead Act until the Secretary of Agriculture has made a final determination that the acts or transactions in question are outside the scope of the Capper-Volstead Act. No such determination shall be considered final until judicial review of such determination has been completed or the time for such review has expired.

RESTRICTIONS OF COMMISSION STUDIES AND INVESTIGATIONS RELATING TO AGRICULTURAL COOPERATIVES

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(1) conducting any study or investigation of any agricultural marketing orders, or

(2) conducting any study, investigation, or prosecution of any agricultural cooperative which meets the requirements of the Act entitled "An Act to authorize association of producers of agricultural products" approved February 18, 1922 (7 U.S.C. 291-292), commonly known as the Capper-Volstead Act until the Secretary of Agriculture has made a final determination that the acts or transactions in question are outside the scope of the immunity conferred by the Capper-Volstead Act or by Section 6 of the Clayton Act (15 U.S.C. 17). The agricultural cooperative shall have a right to judicial review of the Secretary's determination in the federal district court in any district in which it has an office or does business, provided it seeks a review within 30 days of the Secretary's determination.

STATEMENT OF DONALD E. GRAHAM, VICE PRESIDENT AND GENERAL COUNSEL NATIONAL COUNCIL OF FARMER COOPERATIVES

The National Council of Farmer Cooperatives is a nationwide association of cooperative businesses which are owned and controlled by farmers. Its membership includes 122 regional marketing and farm supply cooperatives, the 37 banks of the cooperative Farm Credit System, and 31 state councils of farmer cooperatives. National Council members handle practically every type of agricultural commodity produced in the U.S., market these commodities domestically and around the world, and furnish production supplies and credit to their farmer members and patrons. Two-thirds of U.S. farmers are affiliated with one or more cooperatives. The National Council represents about 90 percent of the more than 6,400 farmer cooperatives in the nation, with a combined membership of nearly 2 million farmers.

The 96th Congress enacted the Federal Trade Commission Improvements Act of 1980 (P.L. 96-252). Section 20 (a) and (b) directed that no funds appropriated for fiscal years 1980, 1981, or 1982 were to be used for the purpose of conducting any study, investigations or prosecutions of any agricultural cooperative for conduct permitted by the Capper-Volstead Act or for the purpose of conducting any study or investigations of any agricultural marketing orders. The National Council urges this Committee to report out a bill which would continue this restriction on the Federal Trade Commission and to further clarify the intent of Congress in this area.

It is essential that language be adopted to prevent farmer cooperatives from being burdened by layer upon layer of authority in an area where the Secretary of Agriculture and the Department of Justice have primary jurisdiction to prohibit illegal conduct.

The administration and use of market orders is within the jurisdiction of the Secretary of Agriculture under the Agricultural Marketing Agreement Act of 1937 (7 U.S.C. 601-602, 608a-608c). Despite the clear delegation of this authority to the Secretary, the Federal Trade Commission's Office of Policy Planning and Evaluation in 1975 recommended that 29 professional man-years be devoted to a detailed study of Federal Agricultural Market Orders for the years 1976-79. This project by the FTC was a needless waste of federal funds because the Department of Agriculture and the Congress constantly review the Agricultural Market Order Programs. The Congress by way of its review of the budget for the Department of Agriculture and through the work of the Committees on Agriculture pays close attention to the function and operations of federal market orders.

These studies by the Federal Trade Commission were also horribly expensive for farmers. In the early 70's, FTC began an investigation of Ocean Spray Cranberries, Inc. (a farmer cooperative which meets the qualifications of the Capper-Volstead Act) and its use of market orders. After nearly 10 years of investigation and a cost to the cooperative of more than $100,000 the investigation was closed without the filing of a complaint. Although this decade long harassment of Ocean Spray was a costly nuisance it was trivial in comparison to what the FTC did to Sunkist Growers, Inc.

It cost Sunkist Growers, Inc. more than $3 million of its farmer/producers money to defend itself against Federal Trade Commission charges. Sunkist was initially investigated in 1974. In 1977, the FTC issued a complaint alleging serious violations of the Federal Trade Commission Act. In 1981—four years later, Sunkist entered into a consent decree with the Commission in which the serious allegations of the initial complaint were not mentioned.

In another instance the FTC filed a complaint against Central California Lettuce Producers Cooperative (a farmer cooperative which meets the qualifications of the Capper-Volstead Act). This antitrust action was argued twice before the Federal Trade Commission which later dismissed the complaint after the United States District Court, Northern District of California ruled that the challenged activities were within the scope of the Capper-Volstead Act. The federal court suit was spawned by the original Federal Trade Commission action.

We know of no action, certainly within the last decade, where the FTC has been successful in its attacks upon farmer cooperatives. Despite its poor record; the Federal Trade Commission persists in its assaults at great expense to cooperatives and their farmer member/owners.

It is difficult for farmers and their cooperatives to comprehend why the Federal Trade Commission has been so intrusive in the affairs of farmer cooperatives in recent years. The expansionist activities of the FTC into market orders and farmer cooperatives are simply a bureaucratic overreaching and are not predicated upon any mandate from Congress.

During the Congressional debates (1919–1922) leading to passage of the Capper-Volstead Act, the question was frequently raised concerning which branch of government or agency would monitor the activities of farmer cooperatives. (See for example 62 Cong. Rec. 2279 et seq.) The House bill contained an explicit delegation of authority to the Secretary of Agriculture (H.R. 13931, H.R. Rep. #939, 66th Cong., 2nd Sess. (1920)). The Senate version substituted the Federal Trade Commission in place of the Secretary of Agriculture in Section 2 of the bill (Sen. Rep. 655, 66th Cong., 2nd Sess. (1920), Sen. Rep. 236, 67th Cong., 1st Sess. (1921)). A dialogue between Senator Pomerene and Senator Walsh, floor leader for opposition to the bill, clearly shows that it was understood that the House bill would delegate complete regulatory authority over cooperatives to the Secretary of Agriculture, (62nd Cong. Rec. 2122 et seq.).

At the end of the Senate debate, Senator King offered an amendment to delegate the regulatory powers contained in the House-passed bill to the Federal Trade Commission rather than the Secretary of Agriculture. His amendment was defeated on a voice vote, (62nd Cong. Rec. 2279).

Going back even further than 1922, when the Clayton Act was under consideration (1914), Congress was mindful of the minimal bargaining power of the individual farmer in the market in which he buys and sells. In order to encourage and promote agricultural associations for mutual help, Congress exempted farmer cooperatives from the application of the antitrust laws under section 6 of that act.

The enactment of section 6 distinctly expressed the congressional policy of treating farmers and their cooperatives differently from industrialists and middlemen. At that time, Congress saw farmers at the mercy of sharp dealers in the sale of their produce. The situation is even more exacerbated today with the vast accumulations of capital by the grocery store chains and the enormous amount of power wielded by the major conglomerates who are heavily involved in the food industry.

It has long been recognized that the strength of American agriculture emanates from the family farm system. Agricultural cooperatives allow the family farmer to keep his independence and decision making on his own farm while yet permitting him to enjoy the economics of scale offered by his cooperative for marketing his farm produce and purchasing his farm supplies.

Erosion of this system would be great news for the giant corporate enterprises that compete with cooperatives but it certainly would be harmful to consumers.

The great expense incurred by cooperatives in reply to the multipage subpena of the FTC, so often issued in the past has been debilitating enough, but most damaging has been the litigation.

Farmer cooperatives, unlike their major corporation competitors that can hire any number of expensive legal counsel to represent them, simply do not have the resources to finance such fights. This makes cooperatives more disposed to settle with the FTC and accept a consent decree despite their innocence of the charges alleged. When more than $1 million a year is being spent for attorney fees and the other incidents of litigation, as was the case with Sunkist, the Board of Directors—all of whom are citrus growers, are disposed to seek an end of the action and accept any consent decree. Since farmer cooperatives operate at cost, all returns the cooperatives receives less those necessary to operate, are returned to the farmer/owners, So additional expenses like attorney fees, come directly out of the farmers' pockets.

The members of a farmer cooperative are in most instances family farmers with relatively modest operations. They are not investors in the cooperative as a stockholder is in a corporation—they actually participate in the business and sit on the board. The products marketed through the cooperative were grown on their farms. Because of the nature of an agricultural cooperative, an action by FTC against a cooperative is in reality an action against the individual grower members. With the depression that presently exists in agriculture, farmers can ill afford to defend themselves in court against their government.

Proprietary competitors of cooperatives frequently point out that some farmer cooperatives have grown into large business enterprises with high sales volume. What they choose to ignore is that these farmer associations are owned by many family farmers. For instance, among the largest cooperatives are:

Farmland Industries	2,287 local co-ops	500,000 farmer/owners.
Associated Milk Producers		26,641 dairy farmers.
Agway, Inc		119,000 farmer/owners.
Goldkist Inc	44 locals	108,000 farmer/owners.
Sunkist Growers, Inc	60 locals	6,500 grower/owners.
Land O'Lakes, Inc	1,258 locals	350,000 farmer/owners.

Why should Congress prohibit the FTC from taking action against farmer cooperatives unless and until the Secretary of Agriculture has made a determination that the alleged conduct is outside the authority granted under the Capper-Volstead Act? The primary reason is that Congress has delegated the responsibility over co-op activity to the Secretary of Agriculture. The reasons given for conferring this duty on Agriculture rather than the FTC comes through in a very clear manner from the debate when Capper-Volstead was enacted. The Department of Agriculture has far greater expertise in matters of agricultural economics than does the FTC. Even today there is no recognized agricultural economist on the staff of the Federal Trade Commission.

Economists recognize that the very nature of agriculture with its atomistic structure, substitutability of products, lack of supply control, the vagaries of nature—pests and disease, seasonality and perishability (of most farm products) etc. make this industry unique. Such factors are not applicable to industrial economics and agricultural economics does not lend itself to the models of industrial production. In short, the FTC is not equipped to do the job and it would be a needless waste of funds to duplicate the efforts of the Department of Agriculture. The layering of authority in this area clearly serves no useful purpose.

The National Council therefore urges Congress to make the restriction on the Federal Trade Commission activities in the area of federal market orders and agricultural cooperatives permanent by adoption of the attached language to amend Section 5(a) of the Federal Trade Commission Act.

[ATTACHMENT]

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STATEMENT OF PROF. DAVID A. RICE

Preliminarily, I wish to identify myself and my interest in the Consumer Subcommittee's review and oversight of the Federal Trade Commission's interpretation and administration of Section 5. I am a Professor of Law at Boston University School of Law* where my work since 1966 has included teaching and research in the fields of marketing regulation, consumer law and advertising regulation. The views set forth in this statement, however are solely my own. They are submitted as the views of an interested member of the public rather than as those of Boston University or any other individual, business, institution or group.

INTRODUCTION

Two fundamental and closely related deficiencies in the 1970s rulemaking exercise of the FTC's "unfair . . . acts or practices" regulatory authority led, in 1980, to the imposition of limits on the agency's exercise of its authority to regulate "unfair . . . acts or practices" and the enactment of procedural safeguards applicable to rulemaking actions. The first problem was a function of the FTC's lack of experience with policy formulation and decisionmaking through the rulemaking process. The second and more fundamental source of difficulty was a product of the statutory "unfair . . . acts or practices" legal standard. It is the latter to which my presentation is principally addressed. However, some preliminary comments on the first factor and its relationship to the definitional problem are in order as part of a necessary sorting out effort and in light of industry proposals which have been made to either withdraw the Commission's Magnuson-Moss rulemaking power or limit its application. Thereafter, my comments—

(1) demonstrate that the proposed FTC consumer unfairness test errs in its failure to define unfair practices in terms of conduct which is prohibited;

(2) show the unsoundness of the FTC's substantial injury test in its own right with particular attention to—

  (a) the definition of cognizable injury,

  (b) the lack of equivalence of costs and benefits to be considered in the proposed benefit-cost test,

  (c) the proposed use of benefit-cost assessment in a manner which is not consistent with the purpose of benefit-cost assessment as a policy analysis method,

  (d) the unsuitability of benefit-cost analysis to the adjudicative process, and

  (e) the inappropriateness in law and economics of the independent injury avoidability test;

(3) suggest the criteria which should be incorporated into a consumer unfairness which does define the conduct to which the statutory prohibition is applicable;

(4) demonstrate the lack of basis for and the inappropriateness of exempting commercial advertising from the consumer unfairness jurisdiction of the Commission, and

(5) address some of the issues related to the late-breaking proposal to redefine the FTC's authority to regulate deception.

THE RULEMAKING CONTEXT

Properly viewed, the alleged incompatibility between rulemaking and the "unfair . . . acts or practices" prohibition of Section 5 is a product of factual association rather than logical compulsion. The moratorium imposed on the regulation of commercial advertising practices through unfairness theory rulemaking proceedings was a wisely chosen temporary measure which allowed time for reflection and alleviated immediate tensions. However, there is no inherent incompatibility between exercise of the FTC's broad substantive authority to regulate unfair practices and the use of its rulemaking power.

The tendency to jointly target criticism against the FTC's rulemaking power and its "unfair . . . acts or practices" regulatory authority is an understandable product of the fact that the FTC during the 1970s chose to use newly established rulemaking power to implement its recently confirmed and ill-defined consumer unfairness regulatory authority. The Commission placed itself in the tenuous position of having to simultaneously work out in two major areas the kinds of problems which inevitably will be encountered when an agency ventures into any one uncharted area. Unfortunately, its imperfect understanding of the nature and requirements of the rulemaking process spilled over and compounded the difficulties inherent in developing the meaning and application of the broad "unfair . . . acts or practices" prohibition. At the same time, the agency's approach to the definition of consumer unfairness following the Supreme Court's 1972 decision in *FTC* v. *Sperry Hutchinson*, 405 U.S. 233, undercut the sound implementation of its rulemaking power.

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*On leave as Senior Research Scholar, Yale Law School, January–July 1982.

It is critical to recognize the existence and implications of marked differences between the rulemaking process, with which the Commission had very little experience prior to the mid-1970s, and the FTC's more familiar mode of case adjudication. The processes differ not only in their focus, but in their character. The adjudicative process focuses upon specific conduct of one or a few parties and is designed to facilitate the submission or proof and argument concerning the application of existing rules of law to the conduct at issue.[1] Rulemaking, on the other hand, typically addresses industry-wide practices and takes as its task the rational formulation of broadly applicable policy based upon a full assessment of the practices at issue and the evaluation of alternative means for attaining identified regulatory goals.[2]

Policy is, of course, evolved through adjudication and conduct is, as one might expect, measured against a legal standard in rulemaking. With respect to policy development, however, it occurs in adjudication in an incremental fashion through a series of adjudicative decisions. In rulemaking, however, policy development is the product of a telescoped and synoptic process. With respect to the assessment of conduct, the adjudicative proceeding is specific in its focus and is oriented toward narrowing and resolving issues of fact in aid of applying existing rules of law. In rulemaking, on the other hand the conduct at issue is typically assessed in broader terms more appropriate to the comparative assessment of industy-wide remedial or other policy options.

The very character of rulemaking dictates that an administrative agency provide a focus which is akin to or substitutes for the focus that the specific facts of the case provide for adjudication. Taking into account the character and purpose of rulemaking, that focus is provided by the clear definition of the policy goals of the proposed rulemaking action in a manner that relates the rulemaking goals to the legislative policies and goals of the agency's statute.[3] Such specification is necessary for the assessment of the effects of the conduct at issue and for the identification and evaluation of alternative policy choices or regulatory actions, including the alternative of taking no regulatory action. FTC rulemaking actions during the mid-1970s generally were not given such a focus.

The lack of necessary focus in FTC rulemaking proceedings probably was, in part, a product of the Commission's lack of experience with rulemaking and its imperfect understanding of the character of that process. More fundamentally, however, it was a function of the agency's quite independent approach to the definition of consumer unfairness. The misreading of *FTC* v. *Sperry & Hutchinson* as a decision dubbing the Commission a knight errant with authority to challenge commercial practices with the infinitely-edged, but kaleidoscopically-fashioned, sword of "public policy" or "public values"[4] rendered it virtually impossible for the agency to adequately articulate the goals of its rulemaking actions and demonstrate how proposed actions related to the legislative policies and goals intrinsic to the FTCA.

The relevance of the rulemaking context to the current consideration of the FTC's authority to regulate "unfair . . . acts or practices" is, in summary, at least twofold. First, the character of the rulemaking process is such that it starkly exposes an administrative agency's failure to articulate a coherent and workable administrative standard for the implementation of its statutory authority. In the absence of such a standard, it is difficult to properly identify the policy goals of a rulemaking proceeding and impossible, in any event, to relate the proposed action to the legislative goals expressed in the statute from which the agency derives its regulatory authority. Second, and equally important, the Commission's 1970s record nevertheless indicates no more than that the FTC should stick to conduct-focused, incremental policymaking through adjudication until such time as it translates the legislative policies and goals of the FTCA into a generally applicable and administratively workable legal standard. That is to say, the 1970s record does not demonstrate that rulemaking implementation of the consumer unfairness prohibition is inherently inappropriate; it indicates only that the manner in which the Commission went about consumer unfairness rulemaking was fundamentally and fatally flawed.

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[1] L. Fuller, "The Forms and Limits of Adjudication," 93 Harvard Law Review 353 (1978).

[2] See generally C. Diver, "Policymaking Paradigms in Administrative Law," 95 Harvard Law Review 393 (Dec. 1981), upon which the comparison between the characteristics of adjudication and rulemaking in this comment generally draws.

[3] Id. at 413–15.

[4] The Supreme Court text relied upon the FTC stated that: ". . . legislative and judicial authorities alike convince us that the Federal Trade Commission does not arrogate excessive power unto itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness, it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws." (405 U.S. at 244)

The Commission, especially in rulemaking, used the analogy and reference to public values as a definitional statement of its basic authority. However, it is quite clear from the Supreme Court's statement that the Court was stating only that the unfairness standard is not wooden, that the FTC may make ancillary reference to policies and values in aid of its implementation of the primary policies and values of the FTCA and related antitrust laws. Indeed, the Court at another point expressly took note that the FTC had not adequately defined its primary legal standard (405 U.S. at 248).

UNFAIR ACTS OR PRACTICES

The preceding discussion of the rulemaking context in which the consumer unfairness issue arose underscores the need to develop a commonly understood general meaning of the "unfair . . . acts or practices" prohibition. Fidelity to the legislative policies and goals that moved Congress to enact the 1914 FTCA and the 1938 Wheeler Lea Act suggests that the translation of the broad statutory language into a more workable administrative standard must satisfy two tests. First, the formulated standard must be framed in terms which are sufficiently broad to permit the Commission to perform the intended function of administering the statute in a dynamic manner that is responsive to changing market conditions and practices.[5] Second, care must be taken, on the other hand, to express the standard in terms which are both consistent with economic policies and goals embodied in the FTCA and indicative of the types of conduct or marketplace effects which are prohibited.[6] With that in mind, I address my following comments to proposed approaches to the problem and, thereafter, to what I regard as a more soundly grounded and workable alternative.

1. *The 1980 and 1982 FTC Policy Statements*

a. The Statements and Their Historical Foundations

The first Commission statement, a December 1980 address by the Commission to Senators John C. Danforth and Wendell H. Ford, set forth a standard framed in terms of two of the three factors identified in the FTC's 1964 Cigarette Advertising and Labeling Rule Statement of Basis and Purpose.[7] The second policy statement, a letter sent to Senators Bob Packwood and Bob Kasten by Chairman James C. Miller III on behalf of the Commission, reiterated the substantial consumer injury standard set forth in the December 17, 1980 letter, but abandoned sub silentio the public policy standard discussed in the December 1980 communication. Public views solicited in connection with March 1982 reauthorization hearings conducted by the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation tended, as might be expected, to adopt the Commission's statements as the point of departure.[8]

Chairman Miller's March 5, 1982 letter to Senators Packwood and Kasten emphasized that the policy goal in the administration of the "unfair . . . acts or practices" prohibition is the prevention of consumer injury. In that regard, he summarized the three factors to be considered in evaluating consumer injury caused by a commercial practice as follows:

> (1) the injury must be substantial; (2) the injury must not be outweighed by any countervailing benefits to consumers or competition produced by the prac-

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[5] See generally D. Rice and B. Keller, "Marketplace Unfairness . . .", in Unfairness: Views on Unfair Acts or Practices in Violation of the Federal Trade Commission Act, U.S. Senate Committee on Commerce, Science and Transportation, 96th Cong., 2d Sess. at 99–104 (1980). See also N. Averitt, "The Meaning of 'Unfair Acts or Practices' in Section 5 of the Federal Trade Commission Act", 70 Georgetown Law Journal 225, 228–39 (1981).

[6] See I. Ehrlich & R. Posner, "An Economic Analysis of Rulemaking", 3 Journal of Legal Studies 257, 258 (1974), stating "A standard indicates the kinds of circumstances that are relevant to a decision on legality . . ." More directly, the authors further state that a standard ". . . is not a list of all circumstances that might be relevant but is rather a criterion by which particular circumstances presented in a case are judged to be relevant or not."

[7] 29 Fed. Reg. 8355 (1964).

[8] See, e.g. Statement of James P. Carty on Behalf of the National Association of Manufacturers at 8–16 (March 18, 1982) and Statement of Martin F. Connor on Behalf of the Chamber of Commerce of the United States at 10–15 (March 19, 1982) Before the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation.

tice; and (3) the injury must be an injury that consumers could not reasonably have avoided.

Reduced to its most pristine form, the tripartite test assumes a threshold determination that some consumer injury is in fact caused by the practice which is under review and then sets forth three factors against which that injury will be gauged in determing whether or not a practice is "unfair".

My first category of concern relative to the propounded approach has to do with the soundness of its foundations. The December 1980 policy statement explicitly represented that the substantial injury test which was later reiterated in Chairman Miller's March 1982 letter was not novel, but merely an experience-based refinement of the substanial injury criterion initially set forth in the 1964 Cigarette Rule standard. The 1980 policy statement further explained that the 1964 test was the necessary point of departure in framing a response to the Consumer Subcommittee's solicitation of the agency's current views because the Surpreme Court, in *FTC* v. *Sperry & Hutchinson,* had quoted the Cigarette Rule factors "with apparent approval" and because the Commission had in fact used and refined the test in practice. Finally, according to the 1980 statement, use of the tripartite 1964 test as the point of departure was proper because the earlier formulation reflected the fact that "[b]y 1964 enough cases had been decided to enable the Commission to identify three factors it considered when applying the prohibition against consumer unfairness."

Starting with the last point, it has been amply demonstrated upon close examination that there were very few, if any, decided consumer unfairness cases upon which the Commission could draw in formulating its 1964 factors.[9] The unfair methods of competition and deception cases upon which the Commission drew in 1964 provided tenuous support at best for the three criteria articulated in the Cigarette Rule Statement of Basis and Purpose.[10] Somewhat ironically, it was only the first-abandoned "immoral, unethical, oppressive or unscrupulous" criterion of the 1964 standard which had some solid support in case law precedents.[11]

The point, in brief, is that the 1964 tripartite test is an unstable foundation which is relevant only if it can be shown that it was shored up subsequent to its initial publication. But that did not in fact occur. Not once did the Commission's briefs submitted to the Supreme Court in the *S & H* case even allude to the 1964 Cigarette Rule test as a statement of agency policy or an interpretation of Section 5. Indeed, it was only in the Sperry & Hutchinson brief that the 1964 test was mentioned and discussed; even when the Cigarette Rule test was so raised, it was totally ignored in the FTC's reply brief.[12] The Commission's behavior in that regard was, of course, quite consistent with the fact that the agency itself rarely cited, let alone applied, the 1964 standard in either pre-*S & H* or post-*S & G* unfairness theory adjudicative or rulemaking actions.[13] It was not, in fact, until controversy erupted in the late 1970's that the Commission began to explain its assessment of challenged practices at least partly in terms of the Cigarette Rule criteria.[14]

Finally, it is well known that a major cause of the controversy that did arise in the late 1970's was that the Commission typically invoked the *S & H* decision for a proposition quite different than the Supreme Court's quotation of the Cigarette Rule factors. Instead of relying upon *S & H* as an indication of Court approval of the 9164 test, the Commission chose to rely on the broad language of the Court in which the agency was likened to a court of equity which could properly consider public values beyond those enshrined in the letter or spirit of the antitrust laws in its administration of the consumer unfairness prohibition.[15]

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[9] See generally D. Rice & B. Keller, note 5 supra at 99. Also see Nelson, "The Politicization of FTC Rulemaking", 8 Conn. L. Rev. 413 (1976).

[10] See Nelson, note 9 surpra at 110.

[11] Notably, *Pfizer, Inc.* 81 FTC 23, 60 (1972) merely acknowledged, in passing, the Supreme Court's quotation of the Cigarette Rule test and went on to propound and apply a quite different analysis. *Pfizer* was, of course, the first unfairness case decided by the FTC after *S & H.*

[12] Upon a review of the briefs, it becomes readily apparent that the Supreme Court's footnote quotation of the Cigarette Rule factors was prompted solely by its concern to answer a question posed in the Sperry & Hutchinson brief, and to do so in a manner that expressed neither approval nor disapproval of the 1964 test.

[13] See generally Rice and Keller, note 4, See also M. Denger, "The Unfairness Standard and the FTC Rulemaking Controversy Over the Scope of the Commission's Authority", and T. Schwartz, "Regulating Unfair Practices Under the FTC Act: The Need for a Legal Standard of Fairness", 11 Akron Law Review 1 (1977).

[14] *Beneficial Corp.,* 86 FTC 119 (1975), enforced in part 542 F. 2d 611 (3d Cir. 1976), cert. denied 430 U.S. 983 (1977) and *Ford Motor Co.,* 94 F.T.C. 564 (1979), set aside on other grounds in *Ford Motor Co.* v. *F. T. C.,* 654 F. 2d 599 (9th Cir. 1981) signaled the rival of the 1964 test in adjudication. Similar signs in the rulemaking area are to be found in the Ophthalmic Goods Rule Statement of Basis and Purpose, 43 Fed. Reg. 23922 (May 24, 1978) and other late 1970's rulemaking proceedings. But consistency was not a hallmark. See, e.g., the subsequent Home Insulation Rule Statement of Basis and Purpose, 44 Fed. Reg. 50218 (Aug. 27, 1979) (Cigarette Rule cited, but analysis framed in terms of *Pfizer*).

The Commission erred seriously when it interpreted *S&H* as indicating that the agency had unbounded jurisdiction to act as the enforcer of public policies and values, whatever their nature and source. It did not err, however, in its initial failure to regard the footnote quotation of the Cigarette Rule standard as an expression of Supreme Court approval of a standard which it expected the agency to henceforth apply. Careful reading of the Court's opinion actually indicates that the Court was careful to preface its footnote quotation of the 1964 test in terms which neutrally described the test as a Commission statement of relevant factors. That the Court's reference was merely descriptive and neither approving nor disapproving was made abundantly clear when the Court remanded the case, explaining that it would not review the application of the consumer unfairness prohibition to Sperry & Hutchinson's trading stamp redemption practices because the record of the case before the FTC failed to set forth necessary findings of fact and, in addition, lacked any statement of the legal standard of unfairness against which fact findings would be assessed.[16] In summary, *S&H* teaches only that "unfair . . . acts or practices" is a statutory prohibition independent of the companion proscriptions against the use of unfair methods of competition and deception and that, incidental to its enforcement of legislative policies and goals reflected in the letter and the spirit of the FTCA and related antitrust laws, the Commission is not precluded from considering other authoritative expressions of public policies and values.

The preceding survey amply demonstrates that neither precedent nor practice dictates, as the Commission's 1980 policy statement suggested, administrative or legislative explication of the "unfair . . . acts or practices" prohibition in terms rooted in the 1964 Cigarette Rule Test. My review does not direct us to the proper formulation. However, it does open the way to a clear and unfettered assessment of the factors set forth in the Commission's 1980 statement and refined in Chairman Miller's March 5, 1982 letter. It is to just such an assessment to which I now turn.

b. The Focus of the FTC's proposed test

My first, and strongest, area of disagreement with the proposed FTC substantial injury test is with its focus. Although there can be no room for disagreement with the view that the Commission's limited resources should be expended solely for the prevention of substantial violations of Section 5, it does not follow that "unfair" and "substantially injurious" are synonymous adjectival modifiers characterizing practices which are in fact violative of the consumer unfairness prohibition.

The proposed consumer injury test provides little guidance to the public, the agency or the courts with respect to the nature of conduct that will be found to violate Section 5. It tells businesses and their legal counsel nothing which would help them make judgments about the legality of a particular practice because it fails to say anything about the legality of conduct in terms of either its type or its effect on the exercise of consumer choice in the marketplace. The most the proposed test accomplishes with rspect to guiding voluntary compliance is to tell a business decision-maker or an attorney that the test lessens the risk of running afoul of Section 5 because it narrows the range of effects which comprise "injury to consumers" and expands the range of considerations which will be regarded as justification for causing injury regardless of its magnitude. Beyond that, the only thing that can be safely said about the potential uses of the test is that it offers virtually unlimited opportunity to raise issues of fact, the resolution of which may drag out FTC proceedings far more than ever before[17] and cripple the agency by forcing it to overinvest its limited resources in a few actions which have been "lawyered" into unduly complex and protracted actions.

The concern that I have with the focus of the FTC policy statement does not reflect or mask a fundamentally different view concerning the legislative goals and policies expressed in Section 5. I find myself in agreement with the Commission and others in viewing the FTCA as a statutory expression of a legislative economic policy to secure the benefits of competitive markets and behavior for competitors and consumers alike. Together with the antitrust laws, the statute provides for regulatory intervention to prohibit or control conduct that is inconsistent with or undermines the effective functioning of competitive markets. The 1938 Wheeler Lea Act neither added to nor subtracted from that basic policy. Rather, it simply added a consumer-focused gauge for assessing the effects of marketplace conduct and ascertaining whether or not identified practices are consistent with the overriding legislative policy. The consumer unfairness standard is, in that respect, one among several statutory metrics for determining if a practice substantially undermines the functioning of competitive markets or exploits imperfect market conditions.

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[15] See, e.g., *Jacob Siegel Co.* v. *FTC*, 327 U.S. 608 (1946); *Beneficial Corp.* v. *FTC*, 542 F. 2d 611 (3d Cir. 1976), cert. denied 430 U.S. 983 (1977).

[16] 405 U.S. at 248.

[17] The problem is sufficiently common in terms of the misuse and abuse of benefit-cost analysis that it is already earned the aphorism of "analysis paralysis". The late 1960s studies of the FTC, of course, revealed serious delay problems which have been a concern of Congress ever since. It also appears that delay and its consequences are of concern to Chairman Miller. See Prepared Statement of Chairman James C. Miller III Before the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation at 9–12 (March 18, 1982).

When viewed in the stated perspective, the definitional task is one which ought to proceed from an examination of the participatory role of consumers in the marketplace. From the perspective of economic theory, the consumer is viewed as policing the market through the exercise of choice among competing offerings in deciding how to spend or allocate limited economic resources. Reasonable or rational exercise of judgment is assumed. Equally, the availability of adequate information upon which to base marketplace decisions is assumed. Drawing upon these fundamental assumptions, it can be stated that effective consumer policing of the marketplace is undermined at least when a practice (1) deprives consumers of adequate information upon which to base market decisions, (2) interferes with the ability of consumers to exercise reasoned judgment or (3) takes advantage of consumers' ability to make informed and rational decisions. Depending upon the circumstances, the resulting injury to consumers may or may not be substantial. But it is the effect of the practice at issue on consumers' effective participation in the marketplace which is the crux of the Wheeler Lea Act amendment and it is that which should be made the focus of the consumer unfairness standard adopted by the Commission or by Congress. A later section of these written comments sets forth some thoughts about the appropriate content of such a standard. Before moving to that, however, there are some concerns which I wish to express about the details of the proposed FTC consumer unfairness test.

c. The content of the FTC's proposed test

1. Economic or monetary harm.—First, the limitation of cognizable injury in all instances to "economic or monetary harm" is decidely too narrow. At least the December 1980 statement took account of the Commission's established practice of reviewing with special care those practices which pose risks to health and safety. It is inappropriate, if not perverse, to require the Commission to find the existence of substantial economic harm incident to a practice which is of the character which I outlined above where the practice poses far larger health or safety risks which consumers cannot discern due to limited capacity (e.g. children) or lack of ability to either discover a latent product condition or assess the risk associated with the use of a containerized or technologically complex product. And while it is all well and good to eschew the role of protecting consumers against offenses to taste or social belief, the greater experience of the courts in dealing with conduct which inflicts emotional distress suggests that it is neither impossible nor inappropriate to take cognizance of such harm in assessing the full extent of economic and directly related harm caused by an actor's conduct.

2. The net benefit test.—The narrow definition of relevant harm is all the more disquieting in light of the Commission's boundless definition of "benefits" which it will weigh against substantial economic injury found to have been caused by a challenged practice. It is a fundamental tenet of benefit-cost assessment that the categories of benefits and costs which are to be weighed against one another must be roughly equivalent in the degree of their relationship to the matter at issue. Confining relevant harm, on one side of the balance, to only direct economic harm and defining cognizable benefits, on the other side, to include every conceivable direct effect and remotely associated externality violates that fundamental tenet and makes a mockery of benefit-cost assessment as a tool of policy analysis.

Quite independently, the introduction of benefit-cost analysis as element of the substantive legal standard of consumer unfairness is an inapt and tortured use of the analytical tool. There can be little argument with the Commission considering, as it deems appropriate, the benefits as well as costs of a commercial practice. But that is not to say that what the FTC is thereby undertaking is beneift-cost analysis in the strict sense.[18] That mode of analysis has never been advanced by profession-

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[18] Perhaps all that the Commission is suggesting is the use of "cost-effectiveness analysis", a distinct form of analysis used to assess alternative means (e.g. remedial choices) for achieving

Continued

als in the field of policy analysis as anything more than a useful tool for the comparative assessment of policy alternatives, an aid to the exercise of the ultimate judgment vested in a decisionmaker.[19] In the context of FTC decisionmaking, its proper place is not in the making of substantive determinations about whether or not a violation has occurred. Rather, its most appropriate sphere is in assessing alternative corrective actions once it has been determined that a practice is of a type prohibited by the act. In that regard, it can be quite useful in implementing the policy axiom that a cease and desist order remedy should be no more restrictive than is necessary to correct the cause of the harm found to exist.[20]

Although I note it only in passing, my greatest concern relative to my immediately preceding comments is with the attempted use of benefit-cost analysis in adjudicative proceedings. The characteristically bounded nature of adjudication has led legal scholars to conclude that the adjudicative process is unsuited to the resolution of the very kinds of multi-faceted or polycentric issues that are commonly assessed with the aid of benefit-cost and other policy analysis methods.[21] The purposes of adjudication and rulemaking are distinctly different and the methods of each reflect that fact. It would be a grievous error to attempt to impose the analytical methods of the latter on the former simply because they work well in the specific setting for which they were designed.

Further regarding the use of benefit-cost assessment, I do commend Chairman Miller and the Commission for taking the position that full-blown formal analysis—for whatever purpose—should not be mandated for every case. The administrative cost of comprehensive, formal analysis can mount quickly; it seems likely that the cost would often outstrip the magnitude of even a substantial economic harm that is the focus of an FTC proceeding. Moreover, insistence upon formal analysis in every instance will unduly complicate adjudicative and rulemaking matters and result in protracted delay in the resolution of open matters. Care must be taken to avoid benefit-cost analysis being converted form a tool for the imporvement of the quality of decisionmaking into a device which compels the inefficient use of agency resources and invites nit-picking, dilatory behavior directed solely toward postponement of final action or the sowing of highly technical grounds for the review of agency determinations.[22] The associated costs are not ones which are desirable in the abstract nor ones which the public ought to be compelled to underwrite throught both taxes and the cost of goods and services.

3. The injury avoidability test.—Finally, I come to the proposed third test that the injury must be one that consumers could not reasonably have avoided. This test, when read together with the requirement that substantial economic harm exist, is tautological. If the Commission in fact subscribes to the economic market theory view upon which it relied in explaining this criterion in its December 1980 statement, it must conclude a fortiori that the substantial economic harm which it finds to exist upon the assessment of a practice under its first factor could not have occurred if it had been one which consumers could reasonably have avoided. It is simply inconsistent to posit that consumers do exercise their capacity for reasoned and informed judgment in economic activity and then, when the facts demonstrate that substantial economic harm has resulted to consumers from the use of practice, place the burden on complaint counsel or rulemaking counsel to negate the possibility that the injury occurred because consumers failed to act in a reasonable manner. The third factor, in effect, stands a fundamental assumption of economic theory on its head and requires proof, before a violation of Section 5 will be found, that the facts in the particular proceeding bear out that assumption.

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identified goals (e.g. redress of an identified harm or statutory violation). See generally E. STOKEY and R. ZECKHAUSER, A PRIMER FOR POLICY ANALYSIS 153-5 (1978). See also W. Rodgers, "Benefits, Costs and Risks Oversight of Health and Environmental Decisionmaking", 4 Harvard Env'l Law Review 191, 201, 204 (1980) (discussing the various forms of analysis loosely characterized as benefit-cost analysis). Legislation, of course, is not a proper place for ambiguous or loose employment of a critical concept or term.

[19] See, e.g., E. STOKEY and R. ZECKHAUSER, A PRIMER FOR POLICY ANALYSIS 135, 158 (1978).

[20] See generally M. Denger, "The Unfairness Standard and FTC Rulemaking: The Controversy Over the Scope of the Commission's Authority", 49 Antitrust Law Journal 78-84 (1981) and C. Hobbs, "Unfairness at the FTC—The Legacy of *S&H*", 47 ABA Antitrust L.J. 1023 (1978).

[21] See L. Fuller, note 1 supra.

[22] "Analysis paralysis" is discussed extensively in the environmental, occupational health and safety, and pollution control literature. The complaint is voiced by opponents of construction and other development projects (criticizing delay caused by environmental and other groups) and-by environmental and public health proponents of pollution standards, etc. (criticizing delay caused by industry opponents).

2. An alternative formulation of the consumer unfairness standard

As I indicated earlier, it is a hollow test of legality that does not attempt to establish a metric against which persons subject to a law, the enforcing agency and the reviewing courts can rationally and consistently assess the legality of conduct in qualitative terms. Some normative statement framed in terms of permissible or impermissible conduct is required.[23] The proposed substantial consumer injury test is not such a statement and does not fulfill the function of providing guidance for the assessment of protean forms of commercial practices. Rather, its definition of cognizable types of injury and its tests of substantiality speak to collateral, albeit important, issues which have meaning only in relation to a substantive standard. They are, in effect, like two slices of bread for a sandwich which has no middle.

The legislative purpose of the Wheeler Lea Act dictates that the formulation of the substantive "unfair . . . acts or practices" standard must be in terms that reflect that statute's aim of authorizing the Commission to assess the lawfulness of practices in terms of their effect on consumer decisionmaking. Consistent with my earlier comments, and drawing upon the general understanding of the role of consumers as marketplace participants, it is my view that a practice is "unfair" from the perspective of the Wheeler Lea Act if it—

Interferes in a material way with the ability of consumers to exercise reasoned judgment; takes advantage of the inability or limited capacity of consumers to make informed or reasoned judgments; or materially deceives consumers or deprives them of adequate information upon which to make informed or reasoned judgments.

For the record, it seems useful to note that these criteria bear some resemblance to—but are not derived from—a statement in Chairman Miller's letter which asserts, as an aside, that the Commission "should confine its activities to curb behavior that takes unfair advantage of consumers" inadequate knowledge in reaching a decision or inability to protect themselves from such behavior".

The three factors are set forth as relevant criteria, not as proposed language for incorporation into an administrative or legislative standard. My limited purpose at this juncture is to advance a conceptual model which reflects the generally held view that deception is a common form of unfairness, accounts for the shading of conduct beyond deception into other forms, and generically defines other forms of conduct which tend to undermine the effective functioning of markets or take advantage of imperfect market conditions. The identified factors, moreover, are consistent with other commentators' identification of the main currents of unfairness decisions.[24]

It bears repeating that, in addition to adequately defining consumer unfairness in normative terms, it is important to define the type and magnitude of injury that warrants the exercise of FTC regulatory authority. My views concerning the Commission's proposals on those two points have already been set forth in some detail. I do not at this point have sufficient time to develop counterproposals relative to the definition of the injury assessment criteria. I am willing, however, to work with the Subcommittee and other interested parties on the formulation of both a normative standard and the related injury criteria.

3. Consumer unfairness and commercial advertising

The three principal advertising industry trade associations have proposed that, regardless of what other action is taken by Congress with respect to the FTC's unfairness jurisdiction, a total exemption from the application of consumer unfairness standard should be created for commercial advertising.[25] The scope of the exemption would go beyond the protection granted by the moratorium and preclude FTC reliance on an unfairness theory in both adjudication and rulemaking actions related to commercial advertising.

The first of the two grounds advanced in support of the sought exemption is that past abuse of the Commission's power necessitates such an exemption. It is reasoned that:

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[23] See sources cited in note 6, supra.

[24] See, e.g., R. Craswell, "The Identification of Unfair Acts or Practices by the Federal Trade Commission", 1981 Wisconsin Law Review 107; N. Averitt, note 5 supra; T. Schwartz, note 13, supra; and B. Boyer, "Defining Unfairness Under Section 5 of the Federal Trade Commission Act" in "Unfairness: Views on Unfair Acts or Practices . . .," note 5 supra at 121. Together with Bruce P. Keller, Esq., I have also developed the relevant background in "Marketplace Unfairness . . .", note 5 supra.

[25] See Joint Statement of the American Advertising Federation, the American Association of Advertising Agencies and the Association of National Advertisers before the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation of 4-14 (March 19, 1982).

Advertising is an art form. It must motivate and persuade or its cost constitutes an economic loss. Advertising must have freedom and elbow room to do its legitimate job. . .[26]

Relative to these comments, the proponents assert that "The threat of a possible unfairness charge operates as an effective chilling, prior restraint on inventiveness and innovation".[27]

The all too apparent answer to the request for exemption is that the very purpose of the current review of the Commission's consumer unfairness regulatory authority is to prevent the recurrence of past practices which undoubtedly produced great uncertaintly for not just the advertising industry. In addition, it is not sufficient to argue that an exemption is warranted because advertising must motivate and persuade, and therefore must have freedom to be creative. Creativity and innovation are essential ingredients of all aspects of marketing, not just advertising. What is more fundamental, of course, is the argument ignores the fact that the reason that Congress initially vested the Commission with the responsibility of interpreting and implementing a broadly-framed statutory standard was to assure that the law would be responsive to change and innovation in commercial practices. Further, when Congress amended the FTCA in 1938, it did so with knowledge that commercial advertising was something over which the Commission had exercised jurisdiction and it presumably intended that the agency have the power to assess and regulate the effects of creative and innovative commercial advertising on the reasoned exercise of consumer choice.[28]

The second argument advanced in support of the proposed exemption for commercial advertising rests upon the fact that constitutional protection has recently been extended to commercial speech. However, the protection so granted is neither unlimited nor protective of all non-deceptive, truthful commercial speech.[29] The decisions of the Supreme Court in no way suggest that Section 5 would be held unconstitutional as a matter of law in its application of the consumer unfairness standard to commercial advertising.

The two grounds advanced by the advertising industry trade associations do underscore, however, the necessity of formulating a consumer unfairness standard in normative terms which give notice and guidance concerning the nature of conduct that is unlawful. Quite understandably, empty standards are ill-regarded in the context of regulations affecting constitutionally protected speech. And the most effective relief, other than an exemption, that can be provided for the uncertainty and unpredictability which the trade associations pointed to in the past administration of Section 5 is to formulate and consistently apply a standard to which the advertising industry can look in assessing legal risks associated with advertising practices and advertisements. Beyond that, Commission adherence to the guidelines established by the Supreme Court with respect to the regulation of commercial speech provide substantial protection for commercial advertising while preserving the FTC's authority to act in specific and occasional instances in which substantial public interest in protecting consumers against harm outweighs the values secured by first amendment protection of commercial speech.

DECEPTION

Rather late in the game, the question of whether or not—and how—the Commission's deception jurisdiction should be redefined has been introduced for consideration. Although I have been unable to thoroughly review the rationale, features and implications of the various proposals, there are some comments which I wish to offer.

My initial remarks address the changes proposed by Chairman Miller in his recent testimony before the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation. He there suggested the incorporation into the law of a requirement that a challenged representation be material to consumers' decisionmaking, that the agency be prohibited from challenging statements or representations of opinion and that the ultimate test be whether or not reasonable consumers, rather than any or some consumers, are likely to be deceived. These proposals, and the suggestion that they be incorporated into legislation, were advanced as his rather than the Commission's views.

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[26] Id. at 10.

[27] Id.

[28] See Rice & Keller, note 5 supra at 102. See also I. Millstein, "The Federal Trade Commission and False Advertising", 64 Columbia Law Review 439 (1964).

[29] See Central Hudson Gas & Electric Corp. v. Public Service Commission of New York, 447 U.S. 557 (1980). Although the recent decision in Matter of R.M.J., — U.S. — (Jan. 25, 1982) makes it clear that the regulation of commercial speech on grounds other than deception will be closely scrutinized, it does not preclude the regulation of trustful, non-deceptive commercial speech where the state has a substantial interest and the restriction is no broader than reasonably necessary to further or effectuate the purpose of regulation.

My first quarrel is with the proposal to implement the changes by legislative action. The Commission has full authority to publish policy guidelines which both direct the activities of staff and offer guidance to industry. Similarly, it can—and ought to—establish case evaluation and selection criteria. Finally, the Commission has the authority and responsibility to interpret Section 5 in formal adjudicative and rulemaking proceedings. Handing the matter to Congress is inexplicable unless, perhaps, the Commission is divided internally and resort to an outside arbiter is viewed as being necessary.

My second general concern is that Chairman Miller's proposals demonstrate a misperception about the nature of legal standards. Their function is not solely to establish boundaries on the exercise of substantive authority. But, as was the case relative to the proposed consumer unfairness standard, the proposed deception legislation fails altogether to establish a metric against which the lawfulness of conduct can be gauged. It deals only with marginalia, but not the essence.

Turning to the specifics of Chairman Miller's proposals, there is nothing wrong in principle with his proposal that the Commission exercise its power only in cases in which a challenged practice has a material influence on consumer decisionmaking. My concern is with the manner in which the proposal was introduced and the extent to which it reflects views advanced in a March 25, 1982 memorandum addressed to Chairman Miller by Timothy J. Muris, Director of the Consumer Protection Bureau. Chairman Miller suggests that the materiality requirement is required to cure the fact that the law does not now require evidence of consumer injury. His point reflects the concern expressed by Mr. Muris with the agency's tendency to rely upon its independent capacity to assess the meaning and deceptive capacity of challenged representations and practices. However, recent literature indicates that Mr. Muris perhaps understates the extent to which the Commission has in fact relied, and increasingly relies, upon extrinsic evidence in its decisionmaking.[30] Further, although Mr. Muris makes it clear that logical inference may be used as an appropriate substitute for direct evidence in making the determination that a claim is material, the bulk of his analysis is susceptible of being interpreted as indicating that the Commission should more often insist upon and more heavily invest its scarce resources in obtaining direct evidence on the point. Imposing any such burden would, in my view, most likely result in an improper allocation of FTC resources and the delivery of less protection to taxpayers at a higher cost.

Chairman Miller's second proposal prohibit the Commission from challenging statements or representations of opinion. The proposal is explained in terms of incorporating the common law rule applicable in actions in which one party seeks to demonstrate that he/she is entitled to recover damages incurred in reliance upon the statement of another. The rule makes eminently good sense in the two-party context because the focal concern of the court is with resolution of the competing rights and interests of two direct-dealing parties. Even so, a review of the reported cases cited in the secondary literature upon which Mr. Muris relied in the memo which provides the background for Mr. Miller's stated position would quite quickly make it apparent that the fact/opinion distinction is not rigorously applied even in the context of common law adjudication. Rather, there is a strong tendency of the courts to attempt to ascertain whether or not, under the circumstances of the case, the statement of representation—regardless of its fact/opinion characterization—materially influenced the complaining party's decision and, if so, whether or not it was reasonable for the person to act upon that statement or representation. The proposal would bar such an assessment in FTC proceedings.

The preceding comments indicate that it would be unwise to prohibit FTC challenges to all statements or representations which are susceptible of being characterized as expressions of opinion. Further reason for rejecting the proposal becomes apparent when one asks the question of why such statements are so widely used in marketing and advertising if, as Mr. Muris suggests, they do not materially influence consumer purchase decisions. If one looks beyond the models and literature of economics to reputable scholarship in the related fields of communication and social psychology, the quite obvious answer is found. Statements or representations of "mere opinion" in fact influence thought and decisionmaking processes through various means, the most simple of which is the implication of underlying facts which support the offering of the opinion.[31]

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[30] See, e.g., Mr. Brandt & I. Prston, "The Federal Trade Commission's Use of Evidence to Determine Deception," 41 Jcurnal of Marketing 54 (1977).

Finally, with respect to the fact/opinion proposal, it must be taken into account that the functions and goals of the common law and the FTCA are really quite different. The common law is retrospective in its view and seeks to redress actual injury which results from the conduct of one person toward another. It is rigorous and narrow in its focus upon what in fact occurred in a given event. The FTCA, however, is prospective in its orientation and has as its goal the prevention of likely injury before it occurs or is compounded by repetition. These fundamentally different outlooks suggest that incorporation of common law rules pertaining to injury caused by the use of fraud or misrepresentation into the jurisprudence of deception under Section 5 ought to occur only after the most careful consideration of the quite different functions of private and public law and an evaluation of the compatibility of a private law rule with the purposes of the public law. The proposed fact/opinion rule transfer in a form not modified to reflect the quite different function of public law in the area of deception would be, in my view, an egregious mistake.

Chairman Miller's third point is not unsound, but it overstates the "problem". There are, of course, laughable precedents—veritable strawmen for those who would criticize the FTC for focusing its resources upon the protection of fools against their own irresponsibility.[32] Any serious observer of the Commission knows, however, that the effect of a practice on incredulous, unthinking fools is not the benchmark that the FTC has employed in practice. And although there are indeed cases in which the Commission earned criticism for issuing orders in the face of evidence that a relatively small percentage of consumers had been or would likely be deceived, an examination of the records and opinions of all decided cases and matters resolved by consent order would demonstrate that such cases become celebrated because they are the exception rather than the rule. To "cure" the "problem" by enacting legislation is purely and simply overkill, a variant on the well-worn cliché about using an elephant gun to kill a mosquito.

Another suggestion that has been made with respect to deception warrants note because it poses even more serious concerns. It has been suggested that in both the deception and unfairness areas that an intent element be incorporated into the law. The effect of such an element, of course, would be to permit forever the use of a challenged practice, regardless of the injury that it causes, if it cannot be demonstrated that the practice was initially used with knowledge or reason to know that it would violate Section 5 and cause economic or other injury to consumers. Once again, the different orientation and functions of public law and private law, from which the intent element is transported, must be taken into account. In that regard, I simply urge you to reflect upon the fact that the advertising industry trade publication, Printers Ink, concluded as far back as 1911—when it proposed a model statute for adoption by the states as the basis for redressing and preventing marketplace deception—that deception in the marketplace is injurious and wrong regardless of whether or not it is the result of intentional or knowing behavior. A rule that would permit even demonstrably evident actual deception or unfairness to be continued with impunity simply because its initial use was innocent would be a travesty on consumers and totally inconsistent with the efforts of Congress to secure to all the benefits of competitive, honest and fair market systems.

STATEMENT OF SEARS, ROEBUCK AND CO.

Current funding for the Federal Trade Commission expires on September 30, 1982. As Congress considers new authorizing legislation for the Commission, the occasion is ideal to enact basic reforms in the statutory framework upon which the Commission operates.

Sears, as a nationwide retailer and advertiser of thousands of consumer products, is extremely interested in the current Congressional proceedings. Below is a synopsis of Sears positions on three important provisions presently contained, or under active discussion, in several pieces of legislation.

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[31] See, e.g., R. Oliver, "An Interpretation of the Attitudinal and Behavioral Effects of Puffery", 13 Journal of Consumer Affairs 8 (1979).

[32] The most frequently noted, but seldom actually applied, case is *Charles of the Ritz Distr. Co. v. FTC*, 143 F. 2d 676 (2d Cir. 1944). Cf. Bristol-Myers Co., 85 F.T.C. 688 (1975).

UNFAIR OR DECEPTIVE ACTS OR PRACTICES

Under Section 5(a)(1) of the FTC Act, the Commission has authority of prohibit "unfair or deceptive acts or practices." The broadness of this language has, in practice, presented problems. It has permitted the FTC staff, with the endorsement of as few as three Commissioners, to characterize almost any conduct that offens their particular sensibilities as unlawful. The Commission has taken the position that by simply exercising its "expertise", it can define the limits of the law without the application of objective standards. As a result of this, and the tendency of reviewing courts to defer to the Commission's "expertise", the Commission and its staff have repeatedly classified conduct as unlawful on the basis of subjective perceptions and personal beliefs, often in disregard of intent or motive and where no adverse economic impact on consumers exists.

The FTC has limited resources. It, like other government agencies, depends on self-regulation by the business community. In giving the FTC no statutory guidance, Section 5 has allowed the Commission staff to engage in this type of subjective activity which makes it virtually impossible for businessmen to determine what is or is not unlawful.

Sears believes, as do many business organizations, that the time has come to provide the Commission with more definitive guidelines on how it is to exercise its "unfair or deceptive" authority. Therefore, Sears urges Congress to more clearly define the proper focus of the Commission's authority in this area by amending Section 5(a)(1) of the FTC Act as follows:

"Unfair or deceptive acts or practices in or affecting commerce are declared unlawful where such acts or practices—

"(i) consist of material representations known to be false or made in reckless disregard of their truth or falsity, or

"(ii) directly cause or may foreseeably result in substantial economic injury to consumers acting reasonably in the circumstances."

In addition, Section 5(b) should be amended by inserting after its fifth sentence:

"Such order shall require such person, partnership or corporation only to discontinue the method of competition or the act or practice which was at issue in the proceeding unless the Commission determines on the basis of substantial evidence that the economic benefit which would result to consumers or to competition from additional relief would outweigh any additional economic cost to consumers or additional burden on competition."

Adoption of this language would provide the Commission with a clear idea of the types of conduct it should commit its limited resources to regulate. Because this language would, to a great extent, eliminate the uncertainty surrounding what is an "unfair or deceptive act or practice," Sears urges its adoption.

REPEAL OF AUTHORITY UNDER SECTION 5(m) (1) (B)

Under Section 5(m)(1)(B) of the FTC Act, the Commission may seek to impose civil penalties of up to $10,000 for each violation against companies who allegedly violate final cease and desist orders entered in proceedings against other firms. Because this section is suceptible to manipulation and abuse—as Commission enforcement actions have already shown it to be—Sears urges that this section be repealed.

Under this Section there is no requirement that a company from which the Commission is seeking civil penalties had actually been a party to or had prior notice of and an opportunity to be heard in the original cease and desist proceeding. All that is required is that the charged company (1) engaged in an act or practice after a cease and desist order with respect to such act or practice has become final and (2) have "actual knowledge" that it is engaging in such conduct.

Section 5(m)(1)(B) raises serious procedural due process and fairness questions due to the manner in which the Commission has implemented its authority under this Section. The Commission has sent out "notice packages" of cases, many of which are twenty, thirty, or even forty years old. Some packages have omitted Commission decisions reversed on appeal which may alter the "law" involved. Many cases included in such packages are stipulated cases which were not fully litigated as to the facts and the law. As a result, the recepients of these "notice packages" have no opportunity to challenge the validity of the Commission's original determinations. Further, in prosecuting cases under this section, the Commission's staff recently has taken the position that all that is required to establish that a charged company had "actual knowledge" of its unlawful conduct is to prove that it received the "notice package" without regard to whether the company factually knew it was engaging in the conduct declared unlawful.

In addition, under the authority of this Section, there exists the distinct potential for manipulation of the administrative process—even when an actual cease and desist hearing is held. The FTC can simply select as a respondent a firm which, because of financial or other reasons, is least able to mount an effective defense. The Commission thereafter can use any cease and desist order entered against such a company—whether or not tested on judicial review—as a conclusive determination of the legality of the practice in civil penalty proceedings against other companies. In this way, the Commission is able to regulate an entire industry which has never been heard on the matter, without utilizing the rulemaking procedures set forth in Section 18 of the FTC Act.

Section 5(m)(1)(B) is substantively and procedurally unfair. The Commission's recent use and misuse of this Section, with its failure to provide basic due process to respondents, underscores the need for its elimination. Sears urges that Congress repeal Section 5(m)(1)(B).

JURISDICTION OVER PROFESSIONALS

FTC Chairman Miller has testified that there should not be any special exemption for state-regulated professionals from Commission investigations, rulemaking or law enforcement activities. Sears agrees and urges that Congress turn back any attempt by professional groups—or any other special interest groups—to secure special exemptions from FTC jurisdiction.

First, the difficulty in defining what is a "professional" argues strongly against any exemptions. For example, if an exemption is given to state licensed doctors, why shouldn't an exemption be granted to state licensed professional auto mechanics or state licensed beauticians? Is it then possible that an exemption for "professional" groups would be extended to any group a state chooses to license?

Professional groups arguing for special treatment ignore the fact that, to date, FTC actions regarding such groups have been deregulatory, rather than regulatory, in nature. For example, in the retail health market the Commission has acted in those instances where studies and empirical data indicate that certain business aspects of professional practice have not enhanced the quality of goods and services but instead have kept prices artifically high. The FTC's record in this area indicates that the Commission's involvement over professionals has resulted in the infusion of competition in the offering of vital health goods and services to consumers. Moreover, it has often resulted in lessening government regulation.

Two good examples are the Commission's "Eyeglasses Rule" concerning state prohibitions and restrictions against the advertising of eyewear and the Commission's development and the issuance of a Model Drug Product Selection Act for adoption by the states, guaranteeing consumers labeling information so they can choose between brand name prescription drugs or less expensive generic ones.

With the service sector the most rapidly growing component of the economy, and with professional services an enormous portion of that sector, it is imperative that the Commission retain authority to ensure competition in the marketplace.

Sears urges that Congress turn back self-serving attempts by professional groups—or any special interest groups—to carve out specific exemptions from the FTC's jurisdiction and reject any attempt to limit the Commission's authority. If any problem can be demonstrated to exist in the professional area, attention should more properly be directed to providing, for example, specificity in Section 5 of the FTC Act concerning "unfair or deceptives acts or practices." Amending the underlying organic statute—not carving out special exemptions for groups—is the answer to any special problems that might exist. A special exemption for the professions is not in the public interest.

Sears urges that Congress adopt this approach and turn its careful attention to the substantive and procedural provisions of the FTC Act.

STATEMENT OF INTERNATIONAL CHIROPRACTORS ASSOCIATION AND AMERICAN CHIROPRACTIC ASSOCIATION

The American Chiropractic Association and the International Chiropractors Association together represent the approximately 23,000 practicing doctors of chiropractic in the United States.

In July 1981, we submittted separate statements to the Subcommittee in its hearings on the Federal Trade Commission's activities concerning the various professions. In those statements, we opposed any exemption of the health professions from the FTC's jurisdiction and from its scrutiny over anti-competitive an monopolistic practices in the health care industry. We reaffirm that position today.

We proposed a Five Point Program to promote competition in the health care industry, we reaffirmed that proposal today.

We stated that state regulation alone was inadequate to assure competition in the health care industry, and that professional self-regulation was often designed principally to maintain a monopoly of the medical component of the health care industry. We reaffirm that position today.

We stated that the consumer pays the price for failure to assure competition in this field and is thereby denied true freedom of choice of health care providers. We reaffirm that position today.

We stated that Section 5 of the Federal Trade Commission Act, and the Commission's rulemaking and adjudicatory functions, enable the FTC to go beyond the Department of Justice activities in this field, and that the FTC is particularly well-equipped to initiate activities which improve competition and increase consumer choice in the health services market. We reaffirm that position today.

We stated that state regulation by itself had been unable to control anti-competitive and monopolistic practices which have impeded the delivery of all forms of health care and have contributed to escalating health care costs nationally. We reaffirm that position today.

We stated, finally, that there is a clear federal interest in maintaining a competitive market for health services. We reaffirm that position today.

S. 1984

Our prior statement were directed to basic principles, rather than to any particular bill before the Committee. We now wish strongly to oppose the enactment of S. 1984 insofar as it may relate to the health-services industry.

Anti-competitive activites in the health services market have had a long history. Since 1943, the Supreme Court of the United States has held that, although it was a professional organization, the AMA was liable under anti-trust laws for unreasonably restraining the business practices of a potential competitor. *AMA* v. *U.S.*, 317 U.S. 519 (1943). And since then the Federal Trade Commission's anti-trust activities have clearly demonstrated a continuing pattern of organizated medical efforts to throttle competition in the health care industry. Such FTC anti-trust actions have been in the public interest, and were necessary to eliminate restraints on inter-and intra-professional competition.

Section 2 of S. 1984 would mean a total exemption from FTC investigation and law enforcement (including traditional anti-trust cases against group boycotts) for all State-regulated professions, their individual members, and their professional organizations, no matter how harmful their anti-competitive or monopolistic practices are to consumers or to vigorous marketplace competition. The operative term in S. 1984 is "conformance with State law." Some State laws apply anti-trust only to goods, not to services, and therefore would not restrain medical boycotts, and anti-competitive activities against chiropractic and the public who are its patients.

Chiropractic's experience with State regulation of the health professions establishes beyond cavil that the mere presence of State regulation does not prevent boycotts and anti-competitive actions openly organized medicine against chiropractic. This is not theory, but long and bitter factural experience.

Our experience has shown that State regulation of the health professsions has been woefully ineffective in preventing illegal and improper anti-competitive or monopolistic practices by competing professional groups which have openly and explicitly sought to eliminate chriopractic as a health care competitor.

The American public pays over $200 billion annually to practitioners of "State regulated" health professions. Public policy requires that the public be protected in the health care field under the anti-trust laws against anti-competitive practices and unfair dealing. Enactment of S. 1984 would subvert that public interest and, in effect, encourage monopolistic practices in health care.

Advocates of S. 1984 have argued that the FTC's activities in the professional services market constitute an overlay of Federal regulation that interferes with and obstructs effective State regulation. We disagree. The intent of Congress in enacting the body of federal anti-trust law, including the Federal Trade Commission Act, was to supplement State law to reach anti-competitive conduct that went beyond the purview of State law. Price-fixing, boycotts, conspiracies in restraint of trade and the like do not recognize State boundaries. Such activities, furthermore, have little to do with the legitimate interest of State governments and professional associations in the regulation of professional services.

We agree with those proponents of S. 1984 who argue that the anti-trust laws should apply only to the "business aspects of professional practice." It is, however, precisely this aspect of professional regulation that has been the sole focus of FTC activity in the past. This activity can in no way be said to be an attempt by the federal government to "regulate" the professions. Instead, such activity reaches those "business aspects of professional practice" which hinder full and free competition in the market for professional services. Consumers of professional services must continue to be accorded the same protection from monopolistic and anti-competitive practices as are those consumers in other sectors of the economy.

PRESIDENT REAGAN'S PROGRAM

The exemption of the health professions from FTC's anti-competitive activities, which would be brought about by S. 1984, flies directly in the face of the Administration's efforts to increase competition in the health care industry. In his Budget this year, President Reagan said that the federal role in health included the need to "promote competition to reduce the rate of inflation in health care costs", *Budget*, p. 5-127. In his *Economic Report* to the Congress, submitted in February 1982, the President stated, in connection with controlling health care costs:

"A major defect of the system is a lack of competitive forces among those who supply health care", p. 148.

This Economic Report complains of:

". . . the dilution of competition in the health care industry and the resultant inefficiencies . . . The lack of competition means that people receive less 'health' for their expenditures . . . It is difficult to quantify this loss of efficiency, but recent estimates place it in the range of $25 billion a year." p. 150.

The Office of Management and Budget, in its supplementary Budget volume "Major Themes and Additional Budget Details," refers to the Administration's—

". . . general effort to restrain health care costs by stimulating competition in the health care industry . . . If competitive forces are to restrain costs, free entry into health care markets is essential. Otherwise, high-cost providers can monopolize health care markets . . ." p. 263

This OMB statement precisely describes the situation involving medicine and chiropractic in the health care market today in the United States. And on May 4, 1981, Secretary of Health and Human Services Richard Schweiker said that "competition is our highest priority in the health care field." Therefore, elimination of the major protector of health care industry competition, the FTC, is contrary to the major policies of the Reagan Administration.

Since the United States Government is the largest purchaser of health care in the nation (e.g., Medicare, VA, CHAMPUS, Federal contribution to medicaid, etc.), it has a direct financial stake in honest and robust competition in the health service market. Competition in this industry can be a major factor in reducing inflation and the Federal budget deficit.

CONCLUSION

For the aforementioned reasons, ACA/ICA oppose enactment of S. 1984. The FTC is the only Federal agency that has a specific mandate to protect health care consumers. The public interest in a truly competitive health services market demands that the FTC continue to exercise its current legal authority to protect the public in its dealings with the health professions. Enactment of S. 1984 would substantially wipe out the protection now afforded to health care consumers against anti-competitive practices and would seriously restrict if not destory the right of health care consumers to freedom of choice of state-licensed health care providers.

Experience has amply demonstrated that State regulation of the health professions and self-regulation by the professions themselves do not protect either the public or the professions from the anti-competitive and monopolistic practices which prevail in today's marketing of health services.

Continuance of FTC's jurisdiction is a minimum necessity for the protection of health care consumers in the United States from monopolies and anti-competitive practices. We therefore oppose enactment of S. 1984 and urge this Subcommittee to reaffirm the FTC's general and specific authority to enhance fair competition in the market for health care services.

STATEMENT OF ENDICOTT PEABODY ON BEHALF OF THE NATIONAL MASS RETAILING INSTITUTE

NMRI

The National Mass Retailing Institute ("NMRI") represents 125 retail companies with thousands of stores spanning the nation. The annual dollar volume of sales of NMRI members approaches $60,000,000,000 (sixty billion dollars).

Retailers are crucial to the United States economy, as they are the final step in the distribution chain of America's goods. In serving the ultimate consumers, retailers must anticipate and respond to the demands of the public. In buying from manufacturers, retailers strongly influence the mix of products offered in our economy and the methods of sales employed to distribute goods. Positioned as they are in the market, retailers are well situated to understand not only the needs of consumers to be protected by consumer protection laws, but the needs of distributors to be protected by the antitrust laws. NMRI respectfully suggests that its views on the government's consumer protection responsibilities and the government's antitrust enforcement policies merit close attention. Accordingly, we submit the following comments on the FTC's role as protector of the consumer and as antitrust guardian of the marketplace.

THE FTC

In principle, and most often in practice, the Federal Trade Commission serves as an invaluable enforcer of consumer protection and antitrust laws. NMRI does not urge this Committee to gut the FTC's authority to police the marketplace. To the contrary, NMRI welcomes a fair and vigorous Federal Trade Commission. However, certain important amendments to the FTC's consumer protection charter warrant passage.

1. Amendments to section 5(a)(1) "Unfair or Deceptive Acts or Practices"

Nearly all who have submitted comments to this Committee, including the Chamber of Commerce, National Association of Manufacturers, American Retail Federation, and even the FTC itself, recommend that Section 5(a)(1) of the Federal Trade Commission Act be amended. NMRI supports amendments to the "unfair" language of Section 5(a)(1) of the FTC Act. The statutory definition of "unfair" should include three elements which the FTC must prove in order to establish a violation under the "unfair" portion of Section 5(a)(1): (1) the consumer injury should be substantial; (2) the injury from the alleged unfair act or practice should outweigh its benefits; (3) the injury to consumers must not be reasonably avoidable by consumers.

NMRI believes that these three elements do no more than codify the basic premise of our economy: consumers act intelligently in their purchasing decisions. The proposed amendments to the FTC Act acknowledge the rational decisionmaking of consumers and prohibit the FTC from second-guessing consumer behavior when the consumer, with knowledge of the consequences of his act, chooses not to avoid those consequences. That is, as Chairman Miller stated in his remarks, "the Commission should confine its activities to curbing [only that] behavior that takes unfair advantage of consumers' inadequate knowledge in reaching a decision on their inability to protect themselves from such behavior." [1]

2. Repeal of section 5(m)(1)(B) and amendments to section 5

At present, Section 5(m)(1)(B) of the Federal Trade Commission Act allows the Commission to impose penalties and behavioral requirements on companies who were not parties to, nor in receipt of, notice and opportunity to be heard in original cease and desist proceedings. That is, the Section allows the Commission to bring an action against any person that the Commission believes is in violation of a cease and desist order entered in prior proceedings against other companies. The only requirement for such a prosecution is that the second company have "actual notice" of the order. The FTC traditionally attempts to prove "actual notice" by the mere mailing of copies of the cease and desist order to members of the industry. In effect, the FTC can promulgate regulations with industry-wide applicability merely by prosecuting a case against the defendant of its choice. The obvious unfairness of that practice merits little further discussion. Accordingly, NMRI recommends repeal of that statutory authority.

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[1] NMRI believes that further scrutiny of the FTC's conduct in enforcing the statutory prohibition on "deceptive acts or practices" is also appropriate. For example, NMRI submitted comments pursuant to the FTC's "Invitation to Submit Written Comments on Possible Revisions to the Guides Against Deceptive Advertising of Guarantees," 45 Fed. Reg. 51836 (August 5, 1980). NMRI contended that the guides are unnecessary in light of the Magnuson-Mass Warrantly Act. NRMI does not presently believe that an amendment to the deception language of Section 5 is necessary but does believe that enforcement of that provision should be examined.

Similarly, Sections 5(1) and 5(m) of the Federal Trade Commission Act allow a civil penalty of up to $10,000 for "each violation" of an order of the Commission. Neither section sufficiently defies "violation." NMRI suggests that this Committee consider two modifications to the violation provisions of the Act: (1) the term "violation" should be defined so that punishment is meted out for single decisions rather than for each and every conceivable consequence of a particular decision; and (2) a cap should be placed on the maximum liability of a company for civil penalties.

3. Federal Trade Commission relaxation of prohibition on resale price maintenance

NMRI is mindful of Senator Kasten's decision that the 1982 FTC reauthorization proceedings should not include any amendments to the Commission's antitrust authority. NMRI is not proposing that the FTC's antitrust powers be abated; to the contrary, NMRI respectfully suggests that the reauthorization process can, and should, serve as a vehicle for requiring the Commission to enforce present antitrust laws.

One such antitrust law that is within the Commission's domain is the rule that resale price maintenance is per se unlawful. Under Section 5 of the Federal Trade Commission Act, the FTC has jurisdiction to prohibit manufacturers from engaging in "unfair methods of competition." From 1911 to the present, the Supreme Court has consistently denounced resale price-fixing as a clear per se violation of both the Sherman Act and the Federal Trade Commission Act.

Indeed, as recently as 1975, Congress reflected its own view that resale price maintenance is undesirable. By enacting the Consumer Goods Pricing Act in 1975 to repeal the McGuire and Miller-Tydings Acts, Congress necessarily endorsed the existing Supreme Court precedent holding that resale price maintenance was per se illegal.

NMRI will not repeat in detail the findings of the 1975 hearings. It suffices to repeat the conclusions: price competition increases sales, adds to consumer welfare, and produces dynamism in the American economy.

As NMRI noted above, retail distributors are the actors best positioned in the marketplace to respond to, and to anticipate, consumers' desires. Retail merchants, not manufacturers, are the most efficient decision-makers on how goods should be priced and marketed. NMRI firmly believes that resale price maintenance by manufacturers works harm on our economy.

Recent statements by Chairman Miller of the Federal Trade Commission suggest that he believes otherwise. Indeed, Chairman Miller suggests that, in certain instances, resale price maintenance enforced by a manufacturer might be a legitimate restraint on trade. By so speculating, Chairman Miller is at stark odds with the teachings of the Supreme Court, the findings of this Congress, and the overwhelming weight of economic and legal theory. NMRI strongly urges this Committee, as part of the reauthorization process, to instruct the Federal Trade Commission to vigorously enforce the law that resale price maintenance is per se illegal.

STATEMENT OF THE AMERICAN VETERINARY MEDICAL ASSOCIATION

The American Veterinary Medical Association (AVMA) submitted a statement for the record in the subcommittee's oversight hearings on Federal Trade Commission regulation of the professions in July, 1981. In that statement, the AVMA explained why the association believes it is not in the best interest of the public or the veterinary profession to permit the Commission to meddle in the long-standing state authority to regulate professional activities.

We emphasized that the FTC is not a proper organization to control the activities of professionals or their associations:

Many activities of a professional are not susceptible to general commercial rules. Unlike the case with merchants and manufacturers, economic concerns are not the principal motivation of a professional; the principles and rules developed by the FTC in commercial contexts are at best poor public policy when transferred to the professional sector.

The existing regulatory mechanisms at the state level work well and are being continually improved. The Supreme Court cases which have opened opportunities for private rights of action against professionals have provided additional "tools." FTC rule-making is not needed.

In contrast to the efficient regulatory efforts of states and individuals, regulatory actions by the FTC can be truly oppressive to small groups of professionals and their associations. As we described in our July, 1981, statement, in the case of the veterinary profession, the FTC efforts provided no benefit to anyone except the lawyers working for the investigators and investigatees. Over a five-year period, the formal FTC investigation, with the attendant studies, interviews, reports, letters, etc., produced no charges against the AVMA or any other veterinary group. Finally, the Commission concluded in June, 1981, that there was no need for its employees to investigate the profession, a year after the Commission announced that it had dropped each of the questions raised in the initial investigative authorization.

Although we know of no active investigation of the veterinary profession by the FTC at this time, we are well aware that another could be initiated at any time. We fear the effect of again being forced to divert hundreds of hours of staff time to respond to trivial inquiries and to spend thousands of dollars on legal fees to protect our rights. If our previous experience is a guide, this could go on for years before any accusations are made. When a relatively small association, such as the AVMA, is the subject of such a "fishing expedition," the normal and productive activities of the association suffer terribly. An FTC investigation can be truly debilitating.

From our experience and fears, we can only conclude that Congress must act to define the parameters of FTC activity. We support H.R. 3722, which offers a straightforward interim solution: The bill would impose a moratorium on new FTC investigations and proceedings involving the learned professions and their associations. We wholeheartedly endorse the similar provisions contained in S. 1984, which is now before this subcommittee.

We ask the subcommittee to consider this question: What is the need for Federal Trade Commission activity in the field of professional activities? We have read many arguments in support of FTC involvement; each supporting argument is a feeble rationale that threatens substantial costs for the public directly or indirectly through the burdens it would place on professionals.

We are not advocating a wholesale exemption for professionals from the antitrust laws. The traditional enforcement activities would not be affected by H.R. 3722 or S. 1984, except as to the role of one of the actors. S. 1984 would not limit the authority of the Justice Department to bring whatever actions it deems advisable under the Sherman Act. Likewise, the Sherman Act offers opportunities for individual claimants that are only beginning to be developed by plaintiffs' attorneys.

The private rights of action are particularly in keeping with the principle of a less-intrusive federal government. The FTC staffers may spin elaborate theories of potential harm to competition which can be cured only by rulemaking, but the validity and effectiveness of the proposed remedies are wholly speculative. In contrast, there must be a bona fide economic stake involved to prompt a private action. We have observed that state and local veterinary associations are being effectively discouraged from anticompetitive acts or practices by the potential of private actions.

Another argument we have read is that, without the FTC activities, there will be little competition among the providers of professional services. There may have been some truth in that assertion 20 years ago, but times have changed, at least in the veterinary profession. In the Sixties, there were major shortages of veterinarians in many parts of the country, but through the joint efforts of the federal government and universities, the number of "seats" in veterinary schools increased by nearly 50 percent between 1970 and 1980. The Bureau of Health Professions in the Department of Health and Human Services projects a surplus of veterinarians within the next few years. The Bureau estimates that that surplus will grow through the year 2000, which is as far into the future as the agency has been willing to predict.

This changing supply situation is having the classic economic effects on prices, as far as we can tell. Veterinarians are becoming ever more aware of the need to attract clients and "market" their services. Market forces are working as an "invisible hand" to bring about more and more price competition. These are hardly symptoms of a "guild" with a tight lock on supply. Price competition among veterinarians is becoming a reality; we are becoming more concerned about growing competitive pressures which may impair the quality of services.

There is also an argument that state regulation permits unduly rigid standards for licensing and unnecessary restrictions on the form of practice. These are subjects which have attracted the attention of the Federal Trade Commission and about which the Commission has taken some action, e.g., the rule on the prescriptions for ophthalmic goods.

This points up an inherent problem with the antitrust laws: The only public policy issue that is considered relevant in an antitrust analysis is the effect on traditional competitive structure. The majority opinion in *National Society of Profession-*

al Engineers v. *United States*, 435 U.S. 679 (1978), explained this principle better than we ever could:

> There are, thus, two complementary categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality—they are "illegal per se"—in the second category are agreements whose competitive effect can only be evaluated by analyzing the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed. In either event, the purpose of the analysis is to form a judgement about the competitive significance of the restraint; it is not to decide whether a policy favoring competition is in the public interest, or in the interest of the members of an industry. Subject to exceptions defined by statute, that policy decision has been made by the Congress. 435 U.S. at 692.

(Although the Court was discussing the Rule of Reason under the Sherman Act, rather than the Federal Trade Commission Act, we understand the antitrust principles to be equally applicable to the two statutes.)

The orientation and mandate of the Commission are focused on economic and commercial questions. This entails the assumption that professional services are essentially fungible, which common sense tells us is not true. The intimate technical and psychological relationship between a professional and his patient or client is different in kind from the relationship between, e.g., a plumber and his customer. Dicta in some Supreme Court decisions (e.g., *Goldfarb* v. *Virginia State Bar*, 421 U.S. 773 (1975)) have acknowledged this truism, but a "defect" in the law prevents the FTC from recognizing it.

The Federal Trade Commission is simply not suited to handle questions of the regulation of professional licensing and practice in a rationale manner. When the prospect of similarly extensive regulation by other federal agencies has arisen (e.g., giving the Department of Health and Human Services authority to establish fees or set standard procedures for physicians), the idea has been promptly dismissed as patently inappropriate for the federal government. We see no meaningful distinction between that and regulation by the FTC.

Sections 2 through 4 of S. 1984 would bring about changes in the FTC's activities directly related to professionals and their associations. We strongly support the enactment of these amendments and believe the nation will be better off when they are law. The other provisions of the bill obviously have far wider implications for U.S. industry, and we are less certain about these proposals. Years of Commission practice, judicial "gloss," and congressional modifications have produced a monumental administrative procedure for Commission action. We question whether the many steps and safeguards in the administrative procedure afford any significant gain in "justice." As long as the Commission's employees are prosecutor, judge, and jury, and we wonder whether all the procedures are merely window-dressing. A party only has assurance of impartiality when he finally emerges from the Commission proceedings in an appeal to the court of appeals. He has already had to spend enormous amounts of time and money in order to be sure he has preserved his rights until he reaches this impartial tribunal. Is it good government policy to perpetuate this elaborate structure?

The AVMA has had the good fortune to have never experienced the FTC adjudicative process first-hand. We are confident that the reforms offered by the first sections of S. 1984 would preclude the association from ever suffering such an experience. These are our principal concerns, but as a collective "citizen," our association also urges the subcommittee to give thorough consideration to the proposition that justice is not served by the current system of administrative adjudication.

We thank you for the opportunity to present our views on this important matter.

STATEMENT OF THE AMERICAN SOCIETY OF INTERNAL MEDICINE

On behalf of the over 17,500 members of the American Society of Internal Medicine (ASIM), I urge the Subcommittee to act favorably on S. 1984, the Federal Trade Commission Amendments of 1981, as part of the reauthorization of the Federal Trade Commission (FTC).

ASIM is a federation of 51 state component societies whose members, by their training and practice, are physicians who are recognized as specialists in internal medicine.

There is much uncertainty at present concerning the proper FTC role with regard to state regulated professions. In recent years, the FTC has greatly expanded its scope of activity and has been investigating and initiating complaints to stop actions that would not normally be considered within the realm of proper agency activity and for which there is no basis in the Federal Trade Commission Act. Examples from the health field include the FTC's proceeding against relative value schedules and principles of ethics developed by professional associations. The high degree of uncertainty which exists with regard to the latter is illustrated by an evenly divided United States Supreme Court decision (*American Medical Association* v. *Federal Trade Commission*, Case No. 80-1690, decided March 23, 1982).

As a result of the present perceived threat of FTC activity, legitimate actions of professional associations in the public interest are stifled. For example, certain self-regulatory programs of the medical profession through which physicians would police their own ranks to ensure high quality and cost-effective medical care are less likely to be implemented for fear of FTC intervention.

It is therefore time for the Congress to act to clarify its intent for the FTC with regard to state regulated professions. By doing so, Congress will limit this agency's actions to those subject areas which the agency was created to address. For this reason, we strongly urge your support of S. 1984. The bill would clearly establish that the FTC has no jurisdiction over state regulated professions or their nonprofit professional associations (section 3).

The limitation on the FTC's jurisdiction does not mean that these professions and associations would not be subject to regulation and legal scrutiny. Rather their actions would continue to be subject to agencies of both federal and state governments which have traditionally regulated them in the public interest. The legislation would only eliminate a layer of unnecessary, duplicative, and often conflicting regulation.

In addition, aside from state and federal regulation that will continue to apply to these professions, each of them has adopted its own ethical standards which guide its members in responsible conduct to clients and to the public. The vast majority of professionals have heeded their ethics and served the public well. Passage of S. 1984 will foster the continuation of self regulation in the public interest. The FTC simply does not have sufficient know-how to assume this role as do the professions themselves.

In conclusion, ASIM urges you to include the provisions of S. 1984 in any FTC reauthorization reported. By doing so, you will be taking an important step toward providing the FTC as well as those who may be affected by its activities with a much needed clarification of its appropriate and intended function with regard to state regulated professions.

STATEMENT OF THE AMERICAN SOCIETY OF ANESTHESIOLOGISTS, INC.

Mr. Chairman and Members of the Committee, on behalf of The American Society of Anesthesiologists, Inc., the following statement is respectfully submitted for inclusion in the hearing record and for your consideration in connection with S. 1984.

The American Society of Anesthesiologists is a non-profit professional organization with approximately 18,500 members, most of whom are physicians throughout the United States engaged in the practice of the medical specialty of anesthesiology. The purposes of the Society are to advance the science and art of anesthesiology and to foster progress in the scientific, educational and professional aspects of the specialty of anesthesiology, all with a view to promoting the best possible patient care in anesthesia.

ASA supports S. 1984 and endorses the position of the American Medical Association and other professional groups with respect to the need for legislation to curb Federal Trade Commission excesses. The Society's position is based on its own experience with the FTC's use of the federal antitrust laws to regulate the medical profession and to make health policy. This experience (which includes involvement in three FTC investigations) makes the Society uniquely qualified to speak to the issues addressed by S. 1984 and aptly demonstrates the need for this legislation.

At the outset, the Society wishes to make it clear that it supports the concept that there should be competition among health care practitioners. It seeks (and S. 1984 provides) for professionals no special exemption from the Sherman Act or the Clayton Act and the pro-competition policy underlying these statutes. What is of great concern to ASA are the repeated, often over-zealous, attempts by the FTC to impose its own notions about health care by means of questionable extensions of its jurisdiction and abuses of its investigative and enforcement procedures—with no apparent regard to the views of other government agencies (including the Department of Health and Human Services) charged with the responsibility for health care policy.

Particularly egregious has been the FTC's abuse of its data gathering and subpoena powers, which abuse is addressed in Sections 4 and 5 of S. 1984. The Society is acutely aware of the need for reform in this area, for in the last five years, it has had to expend almost $300,000 in responding to three burdensome FTC subpoenas and in defending basic rights and principles against unspecified and unfounded charges.

The first FTC subpoena received by the Society provides a clear example of the type of costly "fishing expedition" to which non-profit professional organizations have been subjected. That subpoena was served on the Society in late December 1976 as part of a sweeping, "non-public" investigation of the activities of the AMA and unspecified "others" with respect to the accreditation of medical schools and allied health education programs; the supply of, and definition of fields of practice for, physicians and other health personnel; and "the development of alternative systems of health care delivery." ASA is informed that some 54 other medical specialty societies and medical specialty certifying boards received similar broadly-worded subpoenas. The Society itself spent in excess of $26,000 to respond to that subpoena. It has been estimated (far too conservatively we believe) that some $500,000 was spent by all those subpoenaed in connection with this investigation, apparently for the edification of the FTC staff or because of some unknown suspicions harbored by the FTC. Even at this late date, no report of the results of this investigation is available and there is thus no basis to judge whether the public interest was served by this investigation.

ASA submits that if the FTC had a reasonable basis for suspecting that particular organizations were violating the antitrust laws, it should have targeted those organizations. The FTC's dragnet approach is simply not consistent with basic notions of fairness, particularly when the burdens incurred by those brought within its sweep are considered. This experience alone demonstrates the need for legislation, such as S. 1984, requiring the FTC to justify its issuance of subpoenas before the fact and to make it bear the cost of producing information it desires to assist it in formulating policy.

There is another dimension to the problem which compels the conclusion that reform is needed. The FTC's demonstrated willingness to launch prolonged and expensive investigations, and ability to do so at comparatively little cost to itself, has presented many targeted professional associations with a dilemma—whether to divert limited resources to defending an FTC action or to enter into a consent decree dictated by the FTC staff. ASA has faced just such a choice on two occasions.

Some six months after completing its response to the first FTC subpoena, ASA received from the FTC staff a ten page "request" for information in connection with a "preliminary investigation" of provisions in the Society's ethical guidelines and policy statements relating to the financial aspects of anesthesia practice. This investigation had apparently been prompted by a single complaint against one of ASA's state component societies and was initiated by the FTC staff, rather than authorized by the Commission itself. Much of the requested information was totally unrelated to that specific complaint. Indeed, a significant portion of the request was designed to support the FTC staff's view of its investigatory powers with reference to professional societies, and, the Society was told, did not necessarily represent an inquiry for purposes other than establishing FTC jurisdiction over the Society. Furthermore, the request called for the production of many of the same documents which the Society had submitted to the staff in response to the first subpoena received from the FTC.

At an early stage, ASA was advised by members of the FTC staff that it could avoid the necessity of responding to the requests relating to the jurisdictional issue if it would enter into an agreement admitting the FTC's jurisdiction over the Society. It was also suggested that the entire matter could be disposed of without a further document production if the Society was willing to enter into a comprehensive consent order. Because of the burden of complying with the information request and given the novel and complex legal issues raised, ASA authorized its legal counsel to attempt to negotiate an acceptable consent order agreement.

After almost three months of negotiation, an agreement was reached with the FTC staff attorney assigned to the investigation, only to have the agreement rejected by a mid-level FTC staffer. The principal basis for his rejection of the agreement was ASA's refusal to waive its right under the First Amendment to employ, in the words of one court, "legitimate persuasion and reasoned argument" [1] in advocating advisory, non-binding positions respecting anesthesiologists' compensation arrangements and other issues relating to the quality of patient care in anesthesia. Quite simply, the FTC staff was attempting to limit rather severely ASA's ability to express its views on subjects which affect the public's, as well as its members', interests.

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[1] *American Medical Association* v. *United States*, 130 F. 2d 233, 248 (D.C. Cir.), affirmed, 317 U.S. 519 (1943).

Having reached an impasse, ASA had no alternative but to begin to produce the "requested" information—at its own expense, of course. Fortunately, a new FTC staff attorney with a less ideological approach was assigned to this investigation and a settlement of the matter was reached on terms substantially similar to those proposed by ASA months before. At considerable expense, ASA had to hold the first special meeting of its House of Delegates ever convened in order to approve the settlement. Even so, due to delays in the FTC's internal approval process, the consent order which was a part of that settlement did not become effective until some 16 months after ASA was first advised of the investigation.

As a result of its adherence to principle, ASA, unlike many other medical societies which had been forced by financial considerations to sign FTC consent order agreements, was able to preserve its constitutional rights of collective advocacy and to petition government officials. The importance of this achievement is readily apparent, particularly when one considers that many aspects of an anesthesiologist's practice are affected by governmental health care programs, such as Medicare and Medicaid, and that the matter of health policy is one which remains high on the public agenda. This achievement was not without its cost, however. The Society spent almost $75,000 to resolve this matter and to this day continues to incur costs to comply with the consent order.

The second time ASA had to confront the dilemma posed by a burdensome FTC subpoena occurred just seven months after the FTC gave its approval to the consent order settling the second investigation. This time the FTC served ASA with a 14 page subpoena seeking extensive information concerning the Society's activities with respect to non-physicians (principally nurse anesthetists) involved in the administration of anesthesia. Similar subpoenas were served on six ASA component societies around the country.

Interestingly, the Commission authorized the issuance of the subpoena in June 1978, while approval of the ASA/FTC consent order was pending, but the subpoena was not issued by the staff until late August 1979. Again, many of the specifications of the subpoena requested information previously submitted by ASA in connection with the two prior investigations, including information relating to the issue of FTC jurisdiction over the Society. Further, several of the specifications specifically asked for information concerning the Society's positions on federal and state legislation and regulations, and meetings with or "any actions taken or considered by the Society to influence or provide information to" agencies in the Department of Health, Education and Welfare (now the Department of Health and Human Services).

The precise basis, if any, upon which the FTC premised its investigation is even to this day unknown to the Society. It is known, however, that an FTC representative solicited, through the offices of the American Association of Nurse Anesthetists, information as to "the role of nurse anesthetists in providing anesthesia services and the extent to which they are competent to perform these functions without the direct physical supervision of a physician." The Society believes that the subpoenas resulted from information supplied to the FTC following its solicitation.

Whatever may have been the FTC staff's hope of forcing ASA into a settlement premised on the FTC's view of the proper allocation of the responsibilities for patient care in anesthesia, ASA advised the staff at the outset that it would find no evidence that the Society had unlawfully restrained nurse anesthetists from performing those services for which they are qualified. The staff was also told that the Society would resist any attempt to prevent it from expressing its views on the need for appropriate physician direction and supervision of the administration of anesthesia, as required by state medical practice acts. ASA was vindicated when, some two years later, the Commission closed the investigation.

This time it cost ASA over $180,000 to respond to the FTC subpoena and to defend against FTC notions, of questionable merit, about the possibility of "competition" among physicians and nonprofessionals in the provision of health care. Most of this expense was incurred in hundreds of hours spent searching files and producing thousands of pages of documents, as well as in preparing for two "investigational hearings" conducted by the FTC staff. Despite good faith efforts to comply with the subpoena as expeditiously as possible and with great disruption in the conduct of the routine affairs of the Society, the FTC staff constantly complained about the state of the Society's compliance with the subpoena. At the same time, it took the

FTC staff weeks, and sometimes months, to provide simple written acknowledgments of its receipt of ASA's periodic submissions of documents.

As disturbing as this experience with the FTC has been, it is made all the more unpalatable by the refusal of the FTC to take action to stop anticompetitive practices directed against anesthesiologists by hospitals—even when these hospitals and their state associations are misciting the ASA/FTC consent order in support of these activities. These practices involve the use of exclusive contracts in anesthesiology to foreclose otherwise qualified anesthesiologists from practicing their specialty in a hospital simply because they are unable, or unwilling, to enter into a financial arrangement with a favored physician or group. Not only are anesthesiologists thus denied opportunities to practice, but, more importantly, patients are denied access to alternative sources of the medical service they need. Hospitals have attempted to justify these exclusive contracts on many bases, including on the ground that the ASA/FTC consent order reflects the FTC's view that anesthesiologists should be employed by hospitals.

The ASA/FTC consent order embodies no such policy[2] and ASA and others have brought this perversion of the intent of the order to the attention of the FTC staff. Despite this misrepresentation and in disregard of the serious issues raised by exclusive contracts, the FTC has taken no action. This failure to act can hardly be ascribed to lack of opportunity, for in addition the availability of its own investigative powers, the FTC could (if it wanted) participate in one of the many court cases challenging exclusive contracts which have been brought by individual anesthesiologists. Two of these cases are currently pending before different United States Courts of Appeals and provide excellent opportunities for the FTC to submit amicus curiae briefs clarifying its views—a procedure which FTC Chairman Miller, in a recent letter to this Subcommittee, lamented would be restricted if S. 1984 is enacted. In this context, it is certainly fair to ask why the FTC has aggressively pursued the professions on the slightest provocation, while finding itself unable to act when it is one of the professions (as well as the public) which could benefit from an even-handed application of its policies.

An even fuller appreciation of the wastefulness of the FTC's activities with respect to ASA and other medical societies and of its propensity for intransigence is gained when these activities are assessed in the context of the Society's concurrent defense of a suit brought by the Department of Justice alleging that ASA had violated the Sherman Act by publishing a relative value guide relating to professional anesthesia services. This Subcommittee is already aware[3] that the California Medical Association and other medical societies were forced by the staggering cost of defending an FTC action to sign consent orders withdrawing their relative value guides and severely limiting their ability to present testimony, information and advice on physician fee reimbursement issues to governmental bodies and agents and third party payers responsible for determining health care payment policies. Because of the importance and simple justice of preserving the freedom of anesthesiologists to participate in the development of reimbursement policies (including those of the Medicare and Medicaid programs), ASA vigorously defended against the Justice Department's suit. After four years, the production of thousands of documents and a six-day trial, a federal district court in New York, in the only judicial decision on the legality of a relative value guide, held that the ASA relative value guide did not constitute a *per se* violation of the Sherman Act and, under the applicable "rule of reason" standard of antitrust analysis, did not otherwise violate the Sherman Act.

It cost ASA over $600,000 to prove what the Department of Health and Human Services and many private health insurers already knew and what many told the FTC and the Justice Department was the case—that relative value guides play a valuable role in the third party reimbursement system. Having themselves decided that physician-developed relative value guides were per se illegal price fixing schemes, the FTC and Justice Department simply refused to listen. The FTC even went so far as to refuse to attend a meeting of representatives of the Department of Health and Human Services, the Department of Justice and private groups which a member of Senator Talmadge's staff attempted to arrange to discuss the issues involved and whether legislation authorizing the use of relative value guides was necessary or desirable. Perhaps the best comment on the FTC's and Justice Department's position can be drawn from Judge Duffy's opinion in the *ASA* case:

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[2] The ASA/FTC consent order was designed to assure the freedom of an anesthesiologist to choose whatever arrangement he perfers for the compensation of his professional services, without compulsion from any outside agency. See American Society of Anesthesiologists, 93 FTC 101 (1979) (consent decree).

[3] Hearings on FTC Activities Concerning Professionals Before the Subcommittee for Consumers of the Senate Committee on Commerce, Science, and Transportation, 97th Cong., 1st Sess. (1981), pp. 98–99, 202.

"I find [the] attempt to rely on a *per se* analysis . . . to be much too narrow an approach to the problem at hand." [4]

ASA submits that its experience, and the experience of other professional groups with the FTC's consistently narrow and oppressive approach to health care issues, demonstrates that the Federal Trade Commission should not be involved in regulating the professions. Legislation such as S. 1984 is needed to correct the abuses which have characterized the FTC's involvement with the professions. This legislation will not leave the professions unregulated or open the door to the kind of anticompetitive activity all would agree is inappropriate. The professions will still be subject to state regulation and to the strictures of the antitrust laws. In the medical area, Congress and the executive agencies it has specifically authorized to administer health policy will continue to provide whatever federal regulation is necessary. All that will be eliminated will be the administrative excesses and wasteful duplication which the FTC has imposed on the professions as it sought to expand its authority beyond anything ever contemplated when it was established.

ASA appreciates this opportunity to present its views on this important matter and would be pleased to provide the Subcommittee with such further information as it would find helpful in assessing the need for the enactment of S. 1984.

STATEMENT OF THE AMERICAN RETAIL FEDERATION

The American Retail Federation (ARF) respectfully submits these comments on proposed amendments to the Federal Trade Commission (FTC) Act and certain public statements by its Chairman, James C. Miller, III. We request that these comments be made part of the hearing record.

ARF is a federation of 31 national retail trade associations, state retail associations in 50 states and the District of Columbia, and a number of retail companies. Through its members, ARF represents more than one million establishments. Retail industry sales account for approximately one third of the Gross National Product.

The FTC Act affects virtually every aspect of the retail industry's public dealings, including advertising, sales practices, credit sales and warranties. Retailers are frequently subjected to staff inquiries or official requests for information and materials from the commission. As such, as we feel we are especially well situated to evaluate the Act and its implementation.

Although widely criticized in recent years, the FTC provides an important public function by encouraging an open marketplace, free of the type of commercial misconduct that offends consumers and legitimate businessmen alike. In some areas, regulatory and enforcement authority has been delegated by Congress to the discretion of individuals at the Commission. The result has been uneven, and sometimes unjustifiable, activity by the Commission which yields no real benefit for consumers, while creating an uncertain and costly business climate. We therefore urge Congress to act now to remove the most troublesome uncertainties from the FTC Act and help the Commission refocus its activity away from areas Congress does not intend the FTC to control and in the direction of those practices where limited enforcement resources can best be used.

DEFINE "UNFAIRNESS"

The Commission's statutory authority under section 5 to regulate "unfair" or "deceptive" acts or practices continues to be retailers' primary concern. The Commission's authority is essentially a subjective standard, because there is no statutory definition of "unfairness" to guide the Commission (and those subject to its authority) in determining which practices are unfair. In addition, the Commission's authority with respect to deceptive acts or practices is also broad and ill-defined. Through the use of this amorphous concept, the Commission has the authority to prohibit practices which contravene the standard of "unfairness" held by a majority of the Commissioners then in office. Moreover, when used in adjudicative proceedings (as opposed to the rulemaking context), the unfairness authority can be used by the Commission as a basis for challenging as "unfair" an act which has already taken place. A business which engaged in such a practice without knowledge of the Commission's views as to its "fairness" can find itself defendng a charge that the practice violated Section 5 and, if it is unsuccessful, can be subjected to an order prohibiting not only the practice found to be "unfair" but also—under the FTC's policy of "fencing in" potential violators of the Act—other related practices.

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[4] *United States* v. *The American Society of Anesthesiologists, Inc.*, 473 F. Supp. 147, 161 (S.D.N.Y. 1979). In a footnote to this statement, Judge Duffy further noted his view that the public would not benefit if the ASA relative value guide were struck down.

ARF is pleased to note that Chairman James C. Miller, in recognition of the vague nature of the "unfairness" standard of Section 5, has proposed that Congress amend the statute to further define that term. Chairman Miller's standard would provide some guidance to business as to the types of conduct which the Commission might view as "unfair" by restricting that term to practices which (1) result in substantial economic consumer injury, (2) involve injuries which outweigh the benefits of the practice, and (3) cause consumer injuries which are not reasonably avoidable. We support the inclusion of this standard into Section 5, and believe that the formulation proposed by the U.S. Chamber of Commerce (in its March 19, 1982 statement before this Committee) would accomplish this in a clear and concise manner.

ARF believes, however, that Chairman Miller's proposal, even as articulated by the U.S. Chamber of Commerce, still does not adequately deal with the problem of providing those subject to the Act with advance knowledge of the specific acts which the Commission views as unfair. While the statute, as amended, would provide advance notice of the standards which the Commission will apply in determining whether conduct violates Section 5, it simply does not provide a potential respondent with notice of whether a specific practice common to or prevalent in one industry will be viewed as unfair. ARF believes this problem should be addressed by providing that the FTC may use its authority to define practices as "unfair" only in rulemaking proceedings conducted in accordance with the procedures contained in Section 18(b) of the FTC Act. This requirement would provide all industry members who may engage in a particular practice with notice that the Commission, in effect, proposes to outlaw that practice. All affected parties would have an opportunity to address the merits of the Commission's proposal through testimony, cross-examination and the other administrative procedures contained in the rulemaking procedures of the FTC Act and the Commission's rules, including the right to seek judicial review of any final rule the Commission ultimately promulgated. Equally important, however, once a final rule defining an "unfair" practice had been approved, all industry members would then be placed on notice that the specific practice has been found to be an unfair one and that continuation of it would subject them to enforcement proceedings.

Accordingly, ARF proposes that Section 5(a)(1) of the FTC Act be amended as set forth in Attachment A to this statement.

REPEAL SECTION 5(m)(1)(B)

Section 5(m)(1)(B) of the FTC Act allows the Commission to bring a civil action against *any* person, partnership or corporation it believes has violated a final cease and desist order entered in prior proceedings against *other* companies. This permits the FTC to commence enforcement actions against entities which were not parties to the original proceeding and which, therefore, never had an opportunity to be heard on the matter. Such parties may have engaged in conduct similar, but not identical to, that of the original respondent, or may have engaged in such conduct under different circumstances or with less frequency. The only requirement is that the second company have "actual notice" of the order—usually accomplished by the FTC sending summaries and copies of cases to various industry members. In effect, Section 5(m)(1)(B) turns cease and desist orders into rules of general applicability with none of the due process protections applicable to agency rulemaking under the Administrative Procedure Act and the FTC Act itself.

Section 5(m) allows industry-wide standards (the equivalent of trade regulation rules) to be developed based on the conduct of one target company. The target selected by the FTC might well be the company least able to mount an effective defense—or one which provided no defense at all [1]—because of financial limitations or other problems within that company, but not the industry as a whole. It might also be a company distinguishable from the rest of the industry by reason of egregious conduct which justified the imposition of a broad "fencing in" remedial order not appropriate for other industry members. By carefully selecting a target respondent, the Commission is able to regulate an entire industry which has never been heard on the matter.

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[1] The Commission has sent packages of past cases based on stipulated facts and orders as notice to numerous companies of legal standards which could arguably form the basis for a subsequent enforcement action under Section 5(m) against companies not parties to the original cases.

For all these reasons, ARF urges that Section (5)(m)(1)(B) be repealed.

CLEARLY DEFINE "VIOLATIONS" AND LIMIT TOTAL LIABILITY

Sections 5(l) and (m) of the FTC Act provide that persons, partnerships and corporations found in violation of the Act are liable for civil penalties of up to $10,000 for *each* violation. The term "violation" is not defined in the Act. It has, however, been construed by courts to mean each separate manifestation of wrongful conduct.[2] Thus, one act could actually be composed of millions of separate "violations" with potential civil penalties measured in billions of dollars.

ARF believes that such potential liability is often grossly disproportionate to the seriousness of the offense. It encourages the Commission staff to threaten respondents with huge penalties—and to seek settlements based on such threats—by subdividing simple transactions into component "violations." We accordingly propose that Sections 5(1) and (m) be amended to provide that separate violations are not separate offenses if they are of a similar nature and part of a single transaction of series of transactions.

In addition, ARF submits that a cap be placed on a company's possible monetary liability for civil penalties and suggests $500,000 as an appropriate limitation. This would parallel the civil penalty ceiling in the Consumer Product Safety Act.

REPEAL AUTHORITY TO ENFORCE ECOA AS A TRADE REGULATION RULE

Under Section 4 of the Equal Credit Opportunity Act, 15 U.S.C. § 1691c(c), the FTC is authorized to enforce any Federal Reserve Board regulation promulgated under the ECOA in the same manner as if the violation had been a violation of an FTC trade regulation rule.

The result of this overlapping authority has been a history of abuse by the FTC. The Commission has used the threat of overwhelming civil penalties ($10,000 per violation) to extort consent orders based upon technical violations or honest differences of opinion about the intricate provisions of Regulation B, which implements the ECOA.

ARF believes that the penalty provisions of Section 6 (15 U.S.C. § 169e) of the ECOA are sufficient to deter creditors from violating the Act, as well as to compensate those who might be damaged by a creditor's misconduct. Therefore, ARF requests the amendment of ECOA Section 4 (15 U.S.C. § 1691c(c)) to delete the ability of the FTC to enforce ECOA violations as trade regulation rule violations.

NO EXEMPTIONS FOR PROFESSIONALS

ARF concurs with Chairman Miller's recent statements that there should not be any special exemption for state-regulated professionals from FTC investigations, rulemaking or law enforcement activities.

In the retail health services market, the Commission had acted responsibly in those instances where studies and empirical data indicate that certain business aspects of professional practice have to enhanced the quality of goods and services but instead have kept prices artificially high. ARF believes that FTC involvement over the professionals has resulted in the infusion of competition in the offering of various goods and services to consumers. The following initiatives are examples of Commission activities which have been pro-competitive and deregulatory in nature:

Proposed rulemaking to permit the advertising of prescription drug prices directly to consumers.

Rulemaking, entitled Eyeglasses I, which allows the advertising of prices for ophthalmic goods.

Investigation of restrictive state licensing requirements impacting the ownership of community drug stores.

Development and issuance of a model Drug Product Selection Act for adoption by the states so that consumers have a choice between brand name prescription drugs or a less costly generic prescription item.

Proposed rulemaking, entitled Eyeglasses II, that would remove restrictions against the employment of optometrists by lay corporations, office locations in retail settings, branch office restrictions and the use of trade names by optometrists.

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[2] E.G., *U.S.* v. *Readers Digest Association*, 662 F. 2d 955 (3d Cir., 1981), cert. denied, 50 L.W. 3570 (1982) (in which it was held that the mailing of each of 16 million pieces was a separate violation).

ARF estimates that agency activities such as these have resulted in annual savings of at least $500 million because greater availability of information to make more informed purchasing decisions has lowered prices. The retailing sector of the economy, as one of America's largest employers, is directly affected by increases in the costs of professional services, particularly in the health field. Such expenditures are a major component in the cost of a retail operation and directly affect the cost at which goods are ultimately sold to the consumer. We think the FTC should be allowed to continue its efforts to moderate these costs, and therefore, urge the Committee to reject any proposals that would restrict the FTC's jurisdiction over the professionals.

LIMIT ADVERTISING SUBSTANTIATION ORDERS

The FTC should not have the authority to issue sweeping advertising substantiation orders. The Commission has a record of construing advertising claims in the broadest and most unqualified terms and then requiring companies to substantiate these alleged representations. We feel that the Commission must have some basis for either disbelieving the claims or suspecting that they cannot be substantiated and believing that they have resulted in significant economic injury. Without such a basis, the add substantiation orders are only an expensive nuisance for companies that receive them and a waste of the Commission's resources to review them.

ATTACHMENT

Amend Section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. § 45(a)(1) to read as follows:

"(1) to read as follows

"(1)(A) Unfair methods of competition in or affecting commerce are declared unlawful: *Provided, however,* that no method of competition shall be deemed to be unfair unless it—

"(i) violates sections 1 or 2 of the Sherman Act; or

"(ii) is expressly defined to be an unfair method of competition by federal statute.

"(B) Unfair of deceptive acts or practices in or affecting commerce, where such acts or practices directly cause or may forseeably result in substantial economic injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition, are declared unlawful, provided, however, that a practice shall be treated as 'unfair' only if the Commission shall specifically define it as such in a rulemaking proceeding conducted in accordance with Section 18(a)(1)(B) of this Act."

STATEMENT OF THE AMERICAN COLLEGE OF NURSE-MIDWIVES

The American College of Nurse-Midwives (ACNM) has a very strong interest in the activities of the Federal Trade Commission (FTC). The ACNM supports the FTC's current role in relation to the professions because nurse-midwives, physicians and consumers around the country regularly encounter damaging anti-competitive practices. The ACNM is confident that the FTC could act as an important force in protecting nurse-midwives, physicians and consumers from the deleterious impact of these anti-competitive behaviors. In doing so, the FTC could play a significant and pivotal role in lowering the costs of childbirth and well-woman gynecological care and in opening safe options in health care to women and their families.

Nurse-midwifery care is an example of a health care option which has all the markings of a healthy marketplace competitor: it is in demand, it is cost-effective and it is of high quality. If our society is to have an economic system which allows professional health care services such as those provided by nurse-midwives to flourish, then there is a national obligation to provide a marketplace which supports competition among health care providers.

According to the official ACNM definition, "A certified nurse-midwife is an individual educated in the two disciplines of nursing and midwifery, who possesses evidence of certification according to the requirements of the American College of Nurse-Midwives. Nurse-midwifery practice is the independent management of care of essentially normal newborns and women, antepartally, intrapartally, postpartally and/or gynecologically. This occurs within a health care system which provides for medical consultation, collaborative management, and referral and is in accord with the 'Functions, Standards and Qualifications for Nurse-Midwifery Practice' as defined by the ACNM."

There are approximately 2,500 nurse-midwives in the United States and approximately 220 more graduate each year. Most nurse-midwives practice in association with institutions such as hospitals, clinics, and birthing centers and some offer home birth services.

The American College of Nurse-Midwives (ACNM) is the professional organization of Certified Nurse-Midwives (CNMs) in the United States, representing 85 percent of all CNMs. The ACNM is autonomous from all other professional organizations and speaks for its membership on all issues affecting the practice, education, recognition, legislation and economics of nurse-midwifery. The ACNM collaborates with other professional groups which share its primary concern of quality maternal and infant health care for women and babies and is recognized as an advocate for maternal and child health care issues.

A mounting body of evidence suggest that nurse-midwifery care is cost effective. A study in rural Georgia showed significant improvement in birth outcomes and a decrease in health care expenditures after introduction of nurse-midwifery care.[1] The Childbearing Center in New York City has been found to cost both Medicaid and Blue Cross/Blue Shield considerably less money than traditional in-hospital obstetric care.[2] A recent study comparing charges generated by physician and nurse-midwifery clients in a Salt Lake City hospital showed nurse-midwifery clients had an average of $114 less in charges for a normal birth than did physician clients.[3]

In addition several characteristics of nurse-midwifery care suggest that it is cost-effective. These include nurse-midwive's emphasis on prevention and health education, reduction in infant mortality and morbidity rates, lower cesarean section rates and individualized rather than routine use of expensive technology.

The safety of nurse-midwifery care has been well established in the medical literature. A considerably body of research documents the safety of nurse-midwifery care.[4] All studies have shown that the risk to women attended by nurse-midwives is equal to or lower than the risk to comparable groups of women attended by physicians. In fact, the literature reports striking instances of reduction in infant mortality and morbidity rates after the introduction of nurse-midwifery care.

Certified nurse-midwives are a national resource for which various federal agencies have a legitimate supportive role. Since its introduction into eastern Kentucky in 1925, nurse-midwifery care has reduced infant mortality in numerous urban and rural communities with diverse populations. An ACNM survey, conducted in 1976–1977, showed that nurse-midwives delivered more than one percent of all babies born in the U.S. in one year, approximately 33,000 babies.[5] Because the number of nurse-midwives and the number of clinical practice opportunities have increased greatly since then, it is safe to say that certified nurse-midwives are now delivering at least two percent of all American babies born each year.

Nurse-midwives and their consumers have been on the leading edge of the development of family centered maternity care policies in hospitals. They have pioneered in the development of birthing rooms in hospitals and of out-of-hospital birthing centers, a new form of health care institution. These new policies and new modes of health care delivery have had a salutary economic and clinical impact on how American families receive new babies into their lives.

The federal government has long regarded nurse-midwifery care as an important resource. The government has supported nurse-midwifery education through Title V of the Social Security Act (Maternal and Child Health), the Nurse Training Act and the National Health Service Corps scholarship program. Nurse-midwives have been employed throughout the federal health system on Native American reservations, Maternity and Infant Care projects, Improved Pregnancy Outcome Projects, migrant health projects and in the U.S. Military. The U.S. Air Force has its own nurse-midwifery education program which is affiliated with Georgetown University.

Its long standing support of nurse-midwifery practice and the impact of nurse-midwives on the nation's health lead the federal government to have a legitimate concern about the economic conditions under which nurse-midwives practice. The Federal Trade Commission has shown an interest in the practice of nurse-midwifery and the ACNM supports continuation of the FTC's capability to do so.

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[1] Reid, M. L. and Morris, T. B. Perinatal care and cost effectiveness. Medical Care 17(5):491–500, 1979.

[2] Bennetts, A. B. and Lubic, R. W.: The Free-standing birth centre. The Lancet February 13, 1982, 378–380.

[3] Cherry, T. and Foster, T. C.: Comparison of hospital charges generated by certified nurse-midwives' and physicians' clients. Journal of Nurse-Midwifery 27(1): 7–11 January/February 1982.

[4] American College of Nurse-Midwives: Testimony to the Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce, December 18, 1980.

Both the clinical and the business practice of women's health care have undergone enormous changes in the last decade. Many of these business practice changes reflect the demands of healthy childbearing women and their families. In the 1970's, affluent women began seeking nurse-midwifery care which, until then, had been almost exclusively available only to poor women. Nurse-midwives, who had worked almost exclusively as employees in the public sector, began entering a variety of private practice business arrangements with physician collaborators. Reduction in the length of stay after a normal birth, the use of in-hospital birthing rooms, the advent of out-of-hospital birthing centers and safe, professionally attended home births have also opened a variety of economic and high quality choices to healthy women and their families.

Nurse-midwives and the physicians with whom they collaborate, though small in number, provide the obstetrical and well-woman gynecology market with an impetus which has brought about pro-competitive changes in health care. One extremely clear example of the impact of nurse-midwifery leadership can be found in an FTC report obtained through the Freedom of Information Act. In "Competition Among Health practitioners, The Influence of the Medical profession on the Health Manpower Market," which was written in February 1981, the Commission investigated the Childbearing Center operated in New York City by the Maternity Center Association. The Childbearing Center (CbC) is an out-of-hospital birth center which offers a safe alternative approach to childbirth care. Certified nurse-midwives are the providers of primary health care to women, infants and families at the Center.

The Commission writes:

"Amid all the controversy engendered by the Childbearing Center, there is one point as to which there is near unanimous agreement—the competing service provided by the Center has had a profound, and almost all agree, a positive impact on New York City hospitals specifically, and trends in obstetric care generally. At least partly as a result of the Childbearing Center, many major New York hospitals are working to "humanize" the delivery of obstetric care.

"Thus, in almost five years of operation, the Childbearing Center has overcome numerous obstacles and has demonstrated that safe, efficient care can be provided to low-risk mothers in a contest utilizing teams of physician and non-physician professionals. In so doing, it has increased consumer access to alternative delivery systems. And although the Center itself has tended to attract white, middle-class and highly educated women, it appears that by the Childbearing Center's very presence and the success of its experience, its impact on the competitive marketplace is such that the principles of alternative care will become more available in a variety of contexts and for a variety of socio-economic classes in the years to come.[5]

While numerous federal health institutions have investigated clinical options in women's health and obstetric care, only the Federal Trade Commission has a mandate to look at the economic issues in this volatile and changing market. It would be a tremendous loss for the FTC's investigative and research capabilities to be cut back. The FTC's expertise and resources are necessary if the accurate analysis needed for controlling health care costs is to be developed.

Changes in the business practice of women's health care and the entry of nurse-midwives into the private sector have often been resisted with significant anti-competitive, monopolistic efforts on the part of physicians and hospitals. There is clear evidence that much of the resistance to nurse-midwifery practice stems from a desire to keep competitors out of the marketplace. A 1979 General Accounting Office report, found that physician resistance was one of six factors which lead to a nationwide underutilization of certified nurse-midwives.[6] Several of the other factors, including third party reimbursement and state legislation, have ameliorated since 1979, but resistance remains.

This resistance is also documented in "Nurse-Midwifery: Consumers' Freedom of Choice," the record of a hearing held by the Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce of the U.S. House of Representatives in December 1980.[4] The Committee examined four examples of attempts to block the establishment of private nurse-midwifery practices.

The resistance to nurse-midwifery practice has come from many sources: individual physicians, professional organizations such as medical societies and hosptial departments of obstetrics and pediatrics, public bodies such as state medical practice boards, health and malpractice insurance companies and occasionally from nursing.

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[5] American College of Nurse-Midwives: Nurse-midwifery in the United States: 1976–1977, p. 29.

[6] General Accounting Office: Better Management and More Resources Needed to Strengthen Federal Efforts to Improve Pregnancy Outcome. General Accounting Office, Washington, D.C. 1979.

The form of this resistance is varied. It includes refusal to provide medical collaboration, refusal of permission or privileges for use of hospital facilities, refusal of third party payers to reimburse nurse-midwives, harassment of physicians who support nurse-midwifery practice, requests for unreasonable payments for malpractice insurance and deliberate misrepresentation of the nature of nurse-midwifery practice to the public. The impact of this resistance has been severe enough to cause physicians and nurse-midwives to close their practices. This restraint of trade has also resulted in the filing by nurse-midwives, physicians and consumers of two antitrust cases in federal court in recent months.

The FTC has the capacity to enforce consumer protection and pro-competition laws which are sorely needed to insure that appropriate free enterprise forces can act in the obstetrical and gynecological market. Private suits will, of course, continue to be an option for consumers and nurse-midwives, but restricting the FTC's role vis-a-vis the professions cannot help but have a dampening effect on private actions. In addition, the problem of resistance to nurse-midwifery practice is of sufficient depth and breadth to warrant federal concern.

Nurse-midwifery is a state regulated profession. Nurse-midwives practice under a variety of legal arrangements and nurse-midwifery practice is legal in every state now. In many states the existing mechanisms of state regulation function well; they protect consumers without restricting the practice of nurse-midwifery inappropriately. In other states, however, regulatory agencies have shown a particular vulnerability to pressures from special interest groups. Several state agencies have attempted to enact regulations which go far beyond the appropriate oversight of clinical practice. These over-reaching regulations restrain consumer access to nurse-midwives and restrict the trade of nurse-midwives in two ways. The regulations either reach far beyond appropriate levels of oversight of clinical practice or they reach into the area of business practice with prohibitions which bear no reasonable relationship to protection of consumers.

The Federal Trade Commission has a very important role to play in cases where special interest groups press vulnerable state agencies to enact regulations which prevent nurse-midwives from entering the women's health care market as strong competitors. A federal presence in such cases provides both vital data about the economic implications of proposed regulations and an authoritative resource upon which consumers, nurse-midwives and state agencies can draw for assistance.

Like other health professions, the profession of nurse-midwifery is self-regulating. The American College of Nurse-Midwives sets educational standards and accredits nurse-midwifery education programs. The ACNM develops and administers a national certifying examination for graduates of accredited programs and is a member of the National Council of Health certifying Agencies (NCHCA). The ACNM is one of the few professional organizations which maintains the power to discipline its members. The ACNM can censure, suspend or decertify a certified nurse-midwife who is found by a grievance review panel to be practicing in a manner inimicable to the well-being of mothers and babies.

The ACNM's monitoring of nurse-midwives practice is focused on issues of clinical standards and consumer protection. Nurse-midwives and their collaborating physicians have, unfortunately, experienced harassment from professional organizations who took their private self-regulatory role beyond the scope of clinical concerns to the issue of business arrangements made by physicians and nurse-midwives. The anti-competitive impact of this kind of professional association activity injures consumers, nurse-midwives and physicans. The anti-competitive impact of these supposedly self-regulatory behaviors of professional organizations warrants the scrutiny of the Federal Trade Commission. The American College of Nurse-Midwives would strongly oppose efforts to weaken the FTC's ability to investigate the actions of professional associations which step beyond the boundaries of reasonable clinical considerations.

Consumers are vulnerable to both clinical and economic injuries when receiving obstetrical and gynecological care. The mechanisms which provide redress from economic injuries are tremendously burdensome for nurse-midwives and consumers to undertake. Marketplace regulation is best dealt with in the aggregate, from the perspective of a national agency. The role of the Federal Trade Commission in protecting and enhancing competition in the obstetrical care market should not be weakened; it is a role which individual consumers cannot take on. Protection and enhancement of competition in the women's health care market will result in lower costs to consumers and to federal health programs. These economic outcomes are a national priority and they deserve the resources of a strong Federal Trade Commission to protect them.

Certified nurse-midwives are witness to the rising cost of health care and to the burden these costs place on consumers and health care delivery systems. In nurse-midwifery care there are many models of health care delivery options. Other health care providers and institutions can use these models to find more cost-effective means of providing high quality care which consumers will actively seek. In the resistance to nurse-midwifery practice there is a lesson about the lengths to which entrenched market-dominatng forces will go to smother competition. Until health care providers can more freely and fairly compete in the health care marketplace, monopoly-controlled health care costs will continue to rise.

The creation of a marketplace which supports free, fair competition among professionals while providing reasonable oversight of clinical practice would require the invention of a Federal Trade Commission if one did not already exist. The American College of Nurse-Midwives strongly supports continuation of the FTC's current powers of oversight and enforcment in the health care marketplace.

STATEMENT OF PEGGY CHARREN, PRESIDENT, ACTION FOR CHILDREN'S TELEVISION

INTRODUCTION

Action for Children's Television (ACT) is pleased to have the opportunity to submit this statement to the Senate Committee on Commerce, Science and Transportation regarding the reauthorization of the Federal Trade Commission.

ACT is a national advocacy organization working to promote diversity in children's television programming and to eliminate deceptive and unfair television advertising directed to children. We believe that Section 5 of the Federal Trade Commission Act, which prohibits "unfair and deceptive acts or practices in or affecting commerce,"[1] is vitally important to the integrity of Congressional policy, to the widely supported principle of consumer protection, to the promotion of fair marketplace competition, and to the nation's more than 50 million children. We therefore urge Congress to reject efforts to amend or repeal the existing statutory language of Section 5.

FTC Chairman Miller has recommended that the concept of "unfairness" be statutorily defined as causing "substantial consumer injury" that is not outweighed by any benefits and that could not be avoided by a "reasonable" consumer. In addition, he has urged Congress to limit the parameters of Section 5's concept of "deceptive acts and practices" to factual claims, not "opinion," that are likely both to deceive reasonable consumers and to cause consumer injury. His sole concession to vulnerable consumer groups such as children would be to question "whether the perpetrator knew or should have known that the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived." The advertising industry, recognizing a sympathetic Commission, carries this recommendation one step further, and advocates outright repeal of the "unfairness" standard in Section 5.

ACT maintains that it is essential to retain Section 5's standards of "unfairness" and "deception" as interpreted and defined by judicial opinion and case law, not only for children and other suspectible consumer groups, but for the marketplace itself.

SECTION 5 AND THE MARKETPLACE

The operation of a free and competitive marketplace is an appealing philosophical and practical objective for both Congress and the FTC. However, it need not and will not be promoted by eliminating or restricting traditional and viable mechanisms that protect the consumer. There are certain prerequisites to the marketplace dynamic: the notion of a willing seller and a willing buyer, the existence of an arm's length transaction, a "meeting of the minds," and a relatively equivalent bargaining position between and among the parties. The FTC has stated that it relies on "consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention—to govern the market. We anticipate that consumers will survey the available alternatives, choose those that are most desirable, and avoid those that are inadequate or unsatisfactory."[2] Thus the concept of informed consumer choice has, in recent decades, tempered the archaic notion of "caveat emptor"—"let the buyer beware." This is in large measure a result of governmental recognition that marketplace transactions are no longer a consequence of two relatively equal individuals bargaining over a tangible product. Moreover, when the target consumer or buyer is a child, the notion of "caveat emptor" becomes ludicrous.

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[1] 15 U.S.C. s. 45.

[2] "1980 Statement of Policy on Unfairness," p. 7.

CHILDREN IN THE MARKETPLACE

Mechanisms to protect the consumer, such as Section 5, recognize the inherent inequality of the consumer's position vis a vis the seller or advertiser. If there is a fundamental inequality between the consumer and the seller, how much greater is the disparity when the consumer group is comprised of children.

Economic theory characterizes consumer decisions in the following way. A consumer has a budget constraint—an upper bound on the rate at which money can be expended. The consumer faces a wide variety of goods and services from which to choose, and seeks to pick the bundle satisfying the budget limit that is in some sense "best." In making the selection, the consumer may seek and use information about prices and product attributes. One form of information will be advertising. Because consumers continue in the market for long periods and have memories, sellers will have a limited ability to misrepresent their products. The consumer's experience, education, and reasoning ability will limit severely the potential scope of manipulation. The key assumptions in the conceptualization of how markets operate are, therefore: (1) that consumers know what they want, and (2) that they are capable of reasoning and learning from experience. Of course, there are cases in which these assumptions may not hold (e.g. new, complicated, or infrequently purchased products). In these cases, consumers can be expected to seek information from other sources, such as Consumer Reports or experts.

The "child economy" differs from this conceptualization in several ways. For the most part, children do not make significant purchase decisions subject to a budget constraint; instead, they bargain with parents who control the budget and the expenditure policy of the family. Hence, they do not find themselves persistently in a situation of "trading off" one good thing for another—the classic intellectual exercise that leads to placing personal values and priorities on goods and services. Secondly, as children, they do not satisfy the assumptions about education, experience and rationality that can plausibly be made about adults and which contributes to the capacity to make informed consumer choices.

Both statutory and common law have recognized the unique and special status of children and have afforded them protection against the consequences of their immature acts and judgments. For example, there are legal age limits regarding marriage, voting, working in certain occupations, driving, and seeking and holding office. In the marketplace, the law permits minors to void their contracts to protect them against their own improvident acts as well as against the designs of unscrupulous persons.[3] The prohibition against unfair and deceptive trade practices also protects children. It takes into account the fact that television advertising is the primary vehicle for reaching and persuading children to "participate" in the marketplace, and recognizes their immature cognitive development. The mantle of protection which results from this recognition of children's limitations would be destroyed by amending or repealing Section 5.

CHILDREN'S COGNITIVE DEVELOPMENT AND TELEVISION ADVERTISING

Children and adults perceive and respond to television messages in significantly different ways. Children are not simply small adults: their cognitive abilities develop through several stages over time.[4] This is dramatically illustrated by numerous studies of children's reactions to television commercials.[5] There is general agreement that children place indiscriminate trust in television advertising: they focus on the concrete, the tangible and the immediate as opposed to the abstract; they are often unable to distinguish between fantasy and reality; and they do not understand the persuasive or selling intent in advertising.[6] Accordingly, children are often convinced of the superiority of a product by such factors as the character of hero who touts them. For example, in a recent study, more than half of the 4–7 year olds studied expressed a desire to eat "Cocoa Pebbles" breakfast cereal because Fred Flintstone liked it.[7]

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[3] Wood, "Validity of Transactions With Minors and Incompetents," 1951 U. Ill. L.F. 212, 217 (1951).

[4] Piaget, J. "The Child's Conception of the World" (London: Routledge & Kegan Paul Ltd., 1967) (first published, 1929); Piaget, "The Origins of Intelligence in Children" (New York: International Universities Press, 1952).

[5] See attached bibliography.

[6] National Science Foundation, "Research of the Effects of Television Advertising to Children," 30 (1977).

Of all television audiences, children are the most vulnerable and the least able to understand the exaggerations and ambiguities inherent in persuasive 30-second commercials. It is in order to preserve the ability of private citizens and the government to monitor and check unfair and deceptive practices in areas such as television advertising directed to children that ACT urges the retention of the current Section 5 language.

DECEPTIVE ACTS AND PRACTICES

Chairman Miller's proposal to restrict the contours and parameters of "deception" raises significant problems in the area of television advertising directed to children.

(1) Limiting the potential class of claimants to "reasonable consumers" would eliminate children and other vulnerable groups. The notion of a "reasonable child," given the limitations in cognitive development described above, would not appear to be a legally viable concept.

(2) Equally inappropriate would be subjecting only "factual claims," rather than "opinions," to a Section 5 claim of deception. Television advertising directed to children rarely communicates factual information about price, size or durability; instead, techniques such as magical promises, animation, music, singing and dancing, hero endorsements, authority-figure voice-overs, and guarantees of peer group acceptance are used to entice the child viewer. The very essence of children's television advertising is puffery: there are few, if any, factual claims to distinguish from opinion.

(3) The requirement of consumer injury would demand that consumers evaluate the claim or advertisement for themselves. Given the age, experience and rationality of children, ACT maintains this is patently unreasonable.

(4) As a concession to vulnerable or susceptible consumer groups, the advertiser would be subjected to a test of whether her or she knew or should have known that the practice was deceptive; this places an unconscionable burden on the consumer, and turns the consumer protection intent of Section 5 on its head.

Over the years, FTC orders and judicial decisions have established a legal penumbra surrounding the concept of "deception." With regard to children's television advertising, illusory promises of rapid physical growth [8] and exaggerated performance of toys [9] have been found to be deceptive. The legal yardstick has been the "capacity to deceive."[10] This has been used by both FTC Commissioners and judges to assess the critical factor in each case, i.e. the impact of a particular advertisement on the child audience. However, Chairman Miller's recommendation, "whether or not the perpetrator knew or should have known that the act or practice was deceptive," assesses the state of mind of the advertiser, not the target audience. In cases of deception, one must look at the effect on and potential injury to the deceived, not at the intent or good will of the deceiver.

UNFAIR ACTS AND PRACTICES

Chairman Miller's proposal to redefine the concept of unfairness also raises substantial problems. Clearly children can be exploited and injured by unfair advertising, even if it is not deceptive. Children's vitamin commercials are a case in point. In 1975, citing the voluminous evidence on the hazardous effects of vitamins taken in overdoses. ACT petitioned the FTC for a second time to prohibit such practices. Two years later, the FTC issued a consent order against Hudson Pharmaceutical Corp., declaring that "Spiderman" vitamin advertising to children was an unfair trade practice.[11] It should be noted that nothing in the "Spiderman" vitamin ads was found untrue or deceptive. Chairman Miller might argue that vitamin advertising to children would still be prohibited under a narrowed definition of unfairness that incorporated "substantial consumer injury." However, how many children would need to be injured to tip Chairman Miller's cost/benefit scale in favor of consumer protection? It is to deal with precisely this kind of advertising that the "unfairness" standard in Section 5, which constitutes a legally viable criterion for both the courts and the Commission, must be retained.

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[7] Atkin, "Effects of Television Advertising on Children," Children and the Faces of Television, Palmer and Dorr, ed. (New York, 1980).

[8] *ITT Continental Baking Company, Inc.* v. *FTC*, 352 F.2d 207 (2d Cir. 1976).

[9] *In the Matter of Mattel, Inc.*, 79 FTC 667 (1971).

[10] For example, *In the Matter of Topper Corporation*, 79 FTC 681, 684 (1971); *Thiret* v. *FTC*, 512 F.2d 176, 180 (10th Cir. 1975); *Spiegel* v. *FTC*, 494 F.2d 59, 63 (7th Cir.) cert. denied 419 U.S. 896 (1974).

[11] 89 FTC 82 (1977).

The Supreme Court has had almost 50 years' experience interpreting the concept of unfair practices directed against children.[12] More recently, the Court, in *FTC* v. *Sperry & Hutchinson,*[13] clearly articulated the factors to be considered in determining "unfairness":

" (1) whether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been established by statutes, the common law, or otherwise—whether, in other words, it is within at least the penumbra of some common law, statutory, or other established concept of unfairness; (2) whether it is immoral, unethical, oppressive, or unscrupulous; (3) whether it causes substantial injury to consumers (or competitors or other businessmen.)"[14]

Chairman Miller's proposed statutory redefinition of "unfairness" focuses only on the last of these factors, and hence limits the flexibility and judgment of present and future Commissions and courts to assess unfairness on a case-by-case basis. Indeed, Congress intended that the "unfairness" standard a flexible in order to allow the FTC to respond to changing business practices and to "discover and make explicit those unexpressed standards of fair dealing which the conscience of the community may progressively develop."[15]

ACT believes that the FTC has exercised its unfairness jurisdiction with great care and discretion. It is not a limitless and undefined power. In its examination of whether a practice is unfair, the Commission has stated:

"An unfairness analysis will take into account many basic economic facts and considerations, and will permit a broad focus in the examination of marketing practices. Unfairness is potentially a dynamic analytical tool capable of a progressive, evolving application which can keep pace with a rapidly changing economy. Thus as consumers, products and marketing practices change in number, complexity, variety and function, standards of fairness to the consumer may also change."[16]

Congress must ensure that this useful "analytical tool" remains available to protect consumers.

NEED FOR BOTH UNFAIRNESS AND DECEPTION STANDARDS

The statutory prohibition of "unfair or deceptive acts or practices" has been treated as a unitary standard in many instances because of the inherent difficulty in quantifying deception. Advertising which violates Section 5 of the Federal Trade Commission Act has often been described as being "unfair or deceptive" without any clear delineation between its unfairness and its deceptiveness. This does not suggest vagueness or uncertainty, but rather flexibility, intentionally established by Congress to protect the consumer.

ACT strongly objects to the contention that the current standards of "unfairness" and "deception" are either overbroad or duplicative. As of 1978, "the FTC has never found an advertisement directed at adults to be unfair unless it was also deceptive."[17] However, restricting these standards could mislead and injure consumers. Advertisements depicting unsafe imitable behavior,[18] currently prohibited by the FTC, could well fall outside the scope of a redefinition of "unfairness" or "deception."

Throughout Chairman Miller's proposals, one finds the phrase "reasonable consumer." His consumer is no longer "the ignorant, the unthinking and the credulous,"[19] but is the "reasonable man" of tort and contract law. While the reasonable man standard has an important role to play in assigning liability in tort cases, its introduction into the enforcement of the FTC Act would confuse and disrupt important legal precedents. The courts have made clear that the function of the Commission is to protect those who may be easily victimized by deception and unfairness, not just those who are "reasonable" enough to resist deceptive and misleading claims. Finally, if Congress were to take affirmative action to amend or repeal the established legal concepts of "unfairness" and "deception," it would give advertisers a green light to push the law to its new legal limits. Vulnerable consumers, such as children, the elderly and the terminally ill, would surely be the victims of such changes.

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[12] See, for example, *FTC* v, *Keppel & Bros.*, 291 U.S. 304 (1934).

[13] 405 U.S. 233 (1972).

[14] Id. at 239.

[15] *FTC* v. *Standard Education Society*, 86 F.2d 692, 696 (2d Cir. 1936), rev'd on other grounds, 302 U.S. 112 (1937).

[16] *In re Pfizer, Inc.*, 81 FTC 23, 61 (1972).

[17] "Fairness and Unfairness in Television Product Advertising," 76 *Mich. L. Rev.* 498, 529, n. 168 (1978), emphasis added.

[18] *A.M.F., Inc.*, File No. 782-3025, 1979 Trade Regulation Reports 51,589 (youthful models carelessly riding bicycles on busy streets); *General Foods Corp.*, 86 FTC 831 (1975) (naturalist eating unidentified wild fruits or berries); *Uncle Ben's, Inc.*, 89 FTC 131 (1977) (a child cooking rice on a gas stove).

[19] *Aronberg* v. *FTC*, 132 F.2d 165, 167 (7th Cir. 1942).

THE FIRST AMENDMENT

ACT has consistently and strongly supported the First Amendment's free speech guarantees, including its protection of commercial speech.[20] Nothing in our position regarding the need to retain the unfairness and deception standards of Section 5 impinges on the First Amendment. First of all, deceptive speech is not protected by the First Amendment. Moreover, the notion that the prohibition against unfair acts and practices will create a chilling effect on protected commercial speech is unfounded: the Supreme Court itself acknowledged that commercial speech is less likely to be chilled than noncommercial speech.[21] Nor would the retention of the "unfairness" standard, particularly with regard to children, impede the free flow of accurate product information.

In addition, the Supreme Court expressly reserved judgment in *Virginia Pharmacy* with regard to "the special problems of the electronic media."[22] The nexus of the "special problems" of the broadcast media and the special status of children was addressed by the Supreme Court in a First Amendment context, however, in *FCC* v. *Pacifica Foundation,*[23] when it supported the FCC's prohibition against "indecent" (not obscene) language because "broadcasting is uniquely accessible to children, even those too young to read."[24]

It would appear that the courts and Commission, through careful and considered interpretation of statute, precedent, and public policy, have struck a delicate balance between the rights of the advertiser and the rights of the consumer. We urge that this equilibrium not be upset.

CONCLUSION AND RECOMMENDATIONS

ACT believes that the vigorous authority and jurisdiction of the Federal Trade Commission are essential to the protection of the consumer and the marketplace. We also believe that thoughtful and energetic Congressional oversight is critical to this process. We therefore make the following recommendations with regard to the reauthorization of the Federal Trade Commission:

(1) Congress should retain the existing statutory language in Section 5 that "unfair and deceptive acts or practices in or affecting commerce . . . are declared unlawful."

(2) Congress should ensure that children and other vulnerable consumer groups are protected by such standards;

(3) Congress should continue, through such mechanisms as reauthorization of the Federal Trade Commission, adequate funding, oversight hearings and other legislative initiatives, its long-standing commitment to consumer protection; and,

(4) Congress should support public participation funding in FTC proceedings in order to ensure the active involvement of consumers and interested citizens in the regulatory process.

We appreciate the opportunity to share with you our concerns regarding the reauthorization of the Federal Trade Commission.

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[20] *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748 (1976); but see also *Central Hudson Gas and Electric Corp.* v. *Public Service Commission of New York*, 447 U.S. 557 (1980).

[21] *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council*, supra at 771, n. 24.

[22] Id at 773.

[23] 438 U.S. 726 (1978).

[24] Id at 749.

STATEMENT OF THE NATIONAL RETIRED TEACHERS ASSOCIATION AND THE AMERICAN ASSOCIATION OF RETIRED PERSONS

BACKGROUND

In 1980, Data Resources, Inc. (DRI) completed a study for the Associations on "Inflation and the Elderly." That study found that the average elderly incomes (in aggregate terms) managed to slightly exceed the general rate of inflation from the late 1960s through the late 1970s. Consequently, by 1978, the average income of those over age 65 was about 55 percent of the average incomes of the non-elderly. This progress resulted from the deliberate expansion of government programs, especially social security, in recognition of the extremely high (25-30 percent) elderly poverty rates prevailing at that time. Also, the creation of Medicare, Medicaid and SSI helped a great deal to improve the elderly's economic status.

Despite progress made in raising the elderly's average income levels and reducing poverty among them, there is mounting evidence that inflation has begun to wipe away that progress. Elderly poverty rates, on a steady decline through 1978, increased from 13.9 percent in 1978 to 15.1 percent in 1979 and again in 1980 to 15.7 percent—the largest increase in the elderly poverty rate since the Census Bureau began collecting such data and the highest poverty rate of any adult age group. We believe that the fixed nature of the elderly's income components as well as their inflexible consumption patterns—particularly for food, fuel and medical care—are largely responsible for the substantial increase in the elderly poverty rate.

Moreover, despite the limited growth in the elderly's income during the period 1968-1978, the continuing escalation of the elderly's poverty rate and other statistics demonstrate the disadvantaged position of the elderly relative to the rest of the population. For example, in 1980, while only 9 percent of non-elderly households had annual incomes below $5,000, 26 percent of elderly households had annual incomes below $5,000. Similarly, only 20 percent of non-elderly head-of-households had annual incomes under $10,000, while 56 percent of the elderly head-of-households had incomes in that category. Even adding to their income the cash value of the inkind benefits the elderly receive does not change the reality that the elderly, as a group, generally subsist on low and in many cases wholly inadequate incomes. In 1980, over half of all individuals age 65 and above—more than 13 million people—had an average annual income of less than $5,000.

These factors help to illustrate the concern which the Associations have for seeking to maintain a reasonably stable economy. The elderly, as the result of their extremely vulnerable economic position, are clearly one of the first groups to suffer during the uncertainty of unstable economic conditions, such as periods of high inflation and high unemployment.

As organizations representing the collective interests of over 13 million older Americans, we have an ongoing interest in activities which seek to protect the purchasing power of older persons. Given the fragility of the elderly's position in the marketplace, the Associations have strongly supported the Federal Trade Commission in its efforts to protect consumers from unfair methods of competition and unfair or deceptive trade practices which serve to fuel the fires of inflation. Given their relatively fixed and limited income and the impact that high rate inflation is having on the purchasing power that that income represents, the elderly tend to be hurt the most by unfair, anti-competitive, cost and price promoting practices. In addition, older persons tend to be more vulnerable to and less able to afford the financial hardship of fraud, unfairness, and deception in the marketplace.

At issue, at the present time, are several proposals which we feel would seriously undermine the effectiveness of the FTC. These include the following: (1) proposed alteration of the current law of deception, (2) an attempt to statutorily define unfairness, (3) proposed exclusion of the professions from FTC authority, and (4) reauthorization funding levels.

I. DECEPTION

A. In general

Under current law, any advertisement can be found deceptive "if it has a tendency or capacity to deceive." It is our position that the current definition of deception should remain intact.

Chairman Miller proposed to change this definition by requiring the FTC to establish certain items before a case based on deception could be brought. His requirements are as follows: (1) significant measurable injury to consumers not outweighed by any consumer benefit; (2) a determination that the misleading statements or representations were factual claims and not opinion; (3) a finding that the advertising had a propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising. With regard to vulnerable groups, such as the aged, Chairman Miller proposes that (4) FTC protection could only be accomplished by focusing on whether the perpetrator knew, or should have know, that the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived.

Chairman Miller's attempt to alter the meaning of deception has drawn considerable criticism, especially from other members of the FTC. Commissioner Michael Pertschuk states that "it is not surprising that the law of deceptive advertising has evolved slowly and painstakingly through generations of Commission decisions, subject to the intense and careful scrutiny by the Appellate Courts including the Supreme Court. I believe that most legal scholars would affirm that today the law of deception is relatively well settled and provides solid guideposts for those practitioners who wish to remain in compliance with legal and ethical standards."

Commissioner Patricia Bailey states: "It is no trivial matter to alter 44 years of jurisprudence. If the prohibition on deceptive practices is altered, no matter how benign the intentions of those making the change, the natural assumption of the legal community, including state and federal judges, will be that Congress must have intended somehow to change the actual effect of the law. The inevitable result will be that at least some deceptive practices which are now illegal under current law will become legal, as judges and lawyers are cast adrift from precedent to search for the new law's meaning."

Pertschuk goes on to state that "although it may theoretically be possible to develop a case under Miller's guidelines, it may be as a practical matter impossible to bring. For the expense of developing the evidence Miller wants—especially at the time when we have limited resources—will be prohibitive."

Under Chairman Miller's proposal, it is uncertain whether several FTC cases could have been brought. One is a case involving Anacin's claim that promoted their product as the best pain reliever on the market because it contained an ingredient "most recommended by doctors" for curing minor aches and ailments. The FTC investigated and found the ingredient to be plain aspirin. As a result, it found the ads misleading and deceptive and ordered the campaign halted.

Applying the new Miller criteria to the Anacin case, before the FTC could file suit, it would have to determine that consumers bought the product only because of the ad and that they were adversely affected by their decision—paying substantially more than they would have if they had bought regular aspirin.

Another case which possibly could not be brought under Chairman Miller's proposal is one where the FTC ordered the makers of Fresh Horizons bread to change its advertisements that promoted the bread for its high fiber content. The FTC discovered that what Fresh Horizons failed to mention was that the fiber was not grain fiber contained in most breads, but wood pulp derived from the pulp of trees. The Commission found this omission was misleading and deceptive.

In the Fresh Horizons case, under the new Miller criteria, it would be nearly impossible for the FTC to prove that consumers were harmed by the omission that the fiber was made of wood pulp, because there is no evidence that wood fiber is worse than grain fiber. But even though there may be no physical harm attached, doesn't the public have a right to know what it is purchasing? Doesn't the fact that a particular bread is made from trees instead of from natural grains play a substantial part in the selection process? Aren't there some things consumers need to know about the products they are buying even though the products may not kill them?

The Associations believe that the well established law of deception should be left as it currently stands and that no additions to or deletions from it should be made.

The following is a discussion of each of the elements of deception as proposed by Chairman Miller.

B. Materiality/cost benefit proposal

Chairman Miller proposes that before a case could be brought by the FTC, there must be demonstrated significant measurable injury to consumers, not outweighted by any consumer benefit. S. 1984 proposes that "unfair or deceptive" be limited to acts or practices which "cause substantial consumer injury that outweighs benefits derived from the act." The primary purpose of such a definition is to overrule the current definition of deception since it alters the burden of proof necessary to establish that an act or practice is deceptive. In addition, it opens new vistas for litigation over the proper definition of "substantial injury" or "benefit," and the quantum of proof and acceptable methodologies for establishing values for these new terms. The proposal similarly obscures the precise calculus for determining whether injury is indeed outweighed by costs.

It is our belief that if the cost benefit proposal were enacted, both government and business will expend much time and effort ascertaining the ratio of costs to benefits of a questioned practice. Whatever the result, it is hard to imagine that the investigation and litigation process will be less burdensome with these added features than under present law.

We are less concerned about the size of injury, and far more concerned about basic fairness. We think it is ridiculous to stop to total up a balance sheet, weighing consumers' losses against business' gains when citizens are being cheated, misled, manipulated and shortchanged.

Under Chairman Miller's proposal, in addition to requiring the Commission to measure the dollar cost of misleading statements, he would have the Commission look only at economic injury to consumers. His proposal, however, does not take into consideration such things as consumer expectations (to be able to rely upon advertisers' representations) and competitors' losses (an advertiser's competitor may be harmed in the millions of dollars, while the consumer may suffer the loss of a couple of dollars).

Chairman Miller cites as an example of a case that could not be brought using the cost-benefit proposal—the 1977 Poligrip case. There, the makers of Poligrip falsely claimed that the denture adhesive helps denture wearers eat foods such as apples without dicomfort or embarrassment. Miller states that "this product is cheap, frequently purchased and easy for consumers to evaluate for themselves." As a result, Miller concludes "the FTC is not needed to police the marketplace" in this type of case because consumers will be able to find the deception easily on their own—and with relatively little effect on their pocketbooks.

We disagree. Even though the economic harm to one individual may be relatively small, think of the embarrassment that may have been caused to a grandfather who, at a Sunday church picnic, bit into an apple only to find his teeth drop to the ground when he removed the apple from his mouth. In addition, what Chairman Miller hopes to measure is singular economic harm. What of collective economic harm as a result of thousands who may have purchased the item as a result of the advertisement? Would not this have a profound economic impact upon Poligrip's competitors who suffered a loss as a result of the deceptive claim? In addition, should not a 75-year old widow be able to rely upon the representations of an advertiser who is making a sales pitch directed at her?

In *FTC* v. *Colgate-Palmolive Co.* the Supreme Court confirmed that for an advertisement to be deceptive, the Commission must find that it will be a material factor in a consumer's decision to purchase a product. However, the Court noted that the Commission need not survey the public to support such a finding, but may infer materiality from all the evidence. We believe that a requirement of actual proof of injury beyond that already required is burdensome, impractical, and unnecessary.

C. Fact versus opinion proposal

Under the Miller proposal, the FTC would have to make a determination that the misleading statements or representations were factual claims and not opinions. We strongly object to this. We firmly believe that the proper approach is to look to the effect that a particular representation has upon consumers rather than trying to delineate between fact and opinion.

Our position is predicated upon the premise that in a great number of consumer transactions, the consumers and sellers do not stand on equal footing as to available information. As a result of this "informational imbalance" between consumers and business, consumers are oftentimes prone to believe the representations of the salesperson.

As an example, consider an opinion as to the performance capabilities of a washing machine made by a salesman of 20 years to a grandmother who does washing for 14 grandchildren and has never before purchased a washing machine. Since the salesman obviously knows what he is talking about, the elderly lady is not dealing at an arm's-length transaction with the salesman but must rely upon his representations and opinions, as a result of his longtime experience in the field, as to the capabilities of the machine.

Commissioner Pertschuk voices his criticism of the fact-versus-opinion proposal as follows:

"I know of no case that the Commission has brought challenging opinions except for those cases in which the Commission has alleged that opinions such as those of scientific experts were designed to lead consumers to believe that the opinion was backed by expert knowledge and experience. If Dr. Michael DeBakey, the famed heart surgeon, were to appear in a cigarette ad claiming that in his measured opinion as a surgeon it was his judgment a particular cigarette cured cancer, Miller's amendment would appear to place such opinion testimony beyond the reach of the Commission's policing powers. I simply disagree that there is any sound public policy advanced by doing so."

We also anticipate that the enactment of a fact-versus-opinion proposal would result in a great deal of litigation centering around the question of when opinion becomes a representation of fact. We feel the perferred approach is to leave the definition of deception as it currently is.

D. Reasonableness proposal

Chairman Miller's proposal requires a finding that the advertising had a propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising. We find this proposal unacceptable for a number of reasons.

In the first place, one knowledgeable observer has commented that Chairman Miller's deception proposal and the reasonableness proposal in particular, should be subtitled "The Lawyers' Relief Act of 1982". The primary problem with the reasonable consumer standard espoused by Chairman Miller is that there is none. Predictably it would require years and countless hours of case by case adjudication to define standards of reasonableness, as well as acceptable methodologies of proof. How do you define "reasonableness." Would what's reasonable to a consumer in New England be reasonable to a consumer in Texas? Would reasonableness of consumer conduct be determined for the class of consumers injured by a practice as a whole, or would the law differentiate in degree among various consumers depending on the complexity or sophistication of the product or marketing scheme in relation to the age, intelligence, and prior purchasing experience of the individual consumers in the class?

Foreseeable are clashed of expert psychologists and other behavorial scientists over the arcane question of whether consumers—who might, in a weak moment, be taken in by the deception—should have known better. Chairman Miller's proposal would also impose a new and difficult element of proof which would often shift the focus of litigation from the deceptive act or practice of the business to the conduct of the consumer.

Under longstanding interpretations, a practice is deceptive if it has the capacity to deceive any substantial or appreciable segment of the public. Thus, the FTC and the courts have created a uniform minimum standard of conduct which properly encompasses all likely targets of a marketing effort by a particular business.

This current approach we feel is more acceptable than creating a reasonableness standard.

E. Special protection for special groups proposal

With regard to vulnerable groups, such as the aged, the poor, the uneducated, Chairman Miller proposes that FTC protection could only be accomplished by focusing on whether the perpetrator knew the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived. Average consumers who act reasonably are apparently protected regardless of whether the business knew of the likely deceptive effect of its marketing. Vulnerable consumers who act in an unreasonable or gullible manner, on the other hand, are protected only if the merchant knew or should have known of the effect of the practice. Therefore, ads aimed at the elderly that promote cures for cancer could be attacked under this proposal. While we appreciate Chairman Miller's attempt to provide special protection for special groups, we object to his basic premise—his deception criteria—that brought him to the special protection proposal.

In the first place, this proposal is another one which alters the current burden of proof. Using this proposal, it would be far more difficult for the elderly to bring cases since they would have to prove intent.

In addition, a mens rea requirement has never been an element of deception under Section 5, and appropriately not. The FTC Act is not a criminal statute. It does not punish the sinner, it simply seeks to protect the consumer. Intent is irrelevant to whether consumers may be injured and, consequently, to whether a company should be ordered to cease and desist from deceiving the public. Moreover, intent is enormously difficult to prove. Therefore, while Miller's proposal purports to provide special protection for vulnerable groups, the impact of this proposal would leave such groups far more vulnerable to exploitation than under present law.

Again, it would take years of litigation to restore any semblance of stability or predictability to the law, as the FTC and the courts seek coherent definitions of reasonableness, vulnerability, and knowledge. More importantly, these proposals are designed to substantially reduce the standards of acceptable business conduct. If Chairman Miller's proposal is adopted, the elderly, the sick, the handicapped, the uneducated and other regular targets of deceptive practices will suffer their economic losses in face of defenses of good faith, or lack of intent or knowledge.

II. UNFAIRNESS

A. In general

Section 5 of the FTC Act authorizes the FTC to police "unfair acts or practices affecting commerce." This authority, which has remained relatively unchanged during the past 68 years, was originally granted to the Commission in the FTC Act of 1914.

Chairman Miller, and others, now contend that a departure from this well established precedent is in order, and that the Congress should statutorily define unfairness. Miller proposes the following unfairness definition: (1) the consumer injury should be substantial; (2) the injury from the alleged unfair act or practice should outweigh its benefits; and (3) the harm must be one which consumers could not reasonably have avoided. This definition derives from a 1980 Statement of Policy by the FTC.

What Chairman Miller is proposing—a statutory definition of unfairness—was flatly rejected by the Congress when it created the FTC in 1914. Then, the Congress gave considerable thought to whether a specific list of practices should be proscribed. It was decided that a broad statutory standard should be adopted and that the definition of unfair practices was best left to gradual development by the FTC, subject to review by the Courts.

The Associations agree with the Congress of 1914 and strongly oppose any attempt to statutorily define unfairness. We feel the FTC should be able to apply its unfairness standard just as other agencies carry out their broadly-phrased mandates. In addition, we feel that such broad legal authority is necessary in order for the FTC to be able to respond quickly and flexibly to the changing needs of the marketplace. Why hamstring the FTC with a statutory definition of unfairness so it would be unable to deal with constant change?

At the heart of our argument rests our belief that unfairness is not something that lends itself to a precise, statutory standard. How do you legislate good sense? Since unfairness is one of those "beauty in the eye of the beholder" situations, which beholder do you turn to in order to define what is fair?

We contend that any attempt to define unfairness would be an endless task. This is true because any definition of unfairness that is complete today would be incomplete at the time of enactment into law. And, if complete at the time of enactment, it would soon be outdated through the ingeniousness of the unscrupulous businessman. Therefore, if any definition of unfairness is attempted, the continual burden will be placed upon the Congress to define and redefine, again and again, the concept of unfairness.

In addition, any attempt at a definition would result in endless litigation as to the meaning of each word. It will take virtually years of litigation and subsequent judicial interpretation to ascertain with any degree of certainty exactly what such definition might mean. And, before such certainty could be legally established, think of the resulting uncertainty in judicial proceedings across the nation as to how such standard is to be applied.

The Commission's unfairness authority has proved time and time again an important safety valve for the predatory overreaching of sellers that does not fit neatly within the confines of deception. We feel that to define unfairness or to remove the authority altogether would force the concept of deception beyond its limits in an effort to include fairness.

Through case-by-case adjudications, settlements with individual companies, and the promulgation of trade regulation rules, the FTC has over the years used its unfairness authority to stop a variety of specific commercial practices that do not fit easily within traditional theories of deception.

Over the course of the last eight years, we have worked closely with the FTC in several areas which impact heavily on older Americans. Largely, these efforts were aimed at securing disclosure of full and accurate information in the industries affected to allow consumers to make wise decisions about competing goods and services. While the FTC has several tools at its disposal to insure fair competition, the areas in which we were primarily involved dealt with the issuance of trade regulation rules.

This interest is evidenced in the discussion which follows concerning (1) the proposed Funeral Rule, (2) the Eyeglasses Rule, and (3) the prescription price advertising issue.

B. Proposed funeral rule

The Associations' most active participation in the FTC's rulemaking process has been through the proposed Funeral Rule. This rule would require that consumers be provided itemized price information and would require that unfinished wood boxes or alternative containers be made available to consumers desiring to arrange direct cremation.

Since its inception in 1975, the Associations have actively participated in the development of the proposed Funeral Rule as a result of the interest on the part of our members regarding this subject. Although having gone through numerous revisions, the proposed rule is presently in the Office of Management and Budget where it is being analyzed in a "paperwork review." It is our hope that once the proposed rule clears OMB and is resubmitted to the FTC, it will be presented to the Congress this session for its legislative review.

Almost more than any other rule, the proposed Funeral Rule depends on an unfairness analysis. It could not be issued on the basis of a deception theory alone. While some provisions are based on deception (e.g., bans on misrepresenting legal requirements), the most important provisions of the rule are based on unfairness. In the funeral transaction, the most obvious characteristic is the unequal bargaining relationship between the funeral director and the consumer. Consumers in this transaction are uniquely vulnerable, and it is therefore important for the FTC to restrain funeral directors from taking unfair advantage.

One type of unfairness is using this bargaining power to require consumers to buy goods and services they do not want (or would not choose if they knew they had a choice). Package pricing is one example; requiring consumers who want to buy cremation to also buy an expensive casket is another. The failure to disclose material information can also be an unfair practice.

Under the proposed Funeral Rule, the funeral director's refusal to give price information over the telephone—which is the only practical way consumers can "comparison shop" after a death has occurred— is unfair. Similarly, the funeral director's refusal to disclose the amount of money a consumer could save by not buying services which are not required is unfair, because it prevents consumers from making an informed decision. (Essentially, these types of practices are unfair because they override the free choice a consumer would exercise in an arm's-length transaction.) In addition, the proposed rule also defines as unfair the practice of charging consumers for embalming without prior permission where embalming was not required.

C. Eyeglasses rule

It has been estimated that approximately 96 percent of the elderly buy and use eyewear. This indicated, obviously a higher buyer pattern and higher usage of eyeglasses by elderly persons than the public at large. Therefore, the Associations have followed closely the FTC's rulemaking on the Eyeglasses Rule.

The 1978 Eyeglasses Rule eliminated state prohibitions on the truthful advertising of eyeglasses and eye examinations. Particularly, the FTC sought to prohibit or restrain commercial price advertising for eyeglasses through the rules of a trade association. During the 18 months that the rule was fully in effect, competition in the vision care market increased, and prices declined dramatically for eyeglasses and contact lenses. For example, industry observers cited increased competition in the contact lens market stimulated by the Eyeglasses Rule as the primary reason for a 28 percent reduction in wholesale prices for contact lenses. (Business Week, Nov. 5, 1979, at p. 125) This portion of the Eyeglasses Rule, however, was remanded by the D.C. Circuit Court of Appeals.

The same court, however, upheld a section of the Eyeglass Rule that requires optometrists and ophthalmologists to provide a written eyeglass prescription at the end of each eye examination. This rule seeks to remedy the practice of denying consumers copies of their eyeglass prescriptions after an eye examination, or charging an extra fee for their release, so as to discourage comparative shopping for eyeglasses.

More recently, the FTC, on January 13, 1982, published a proposed amendment to the Eyeglasses Rule. In this proposal, the FTC seeks to remedy restrictions that may significantly harm consumers by maintaining higher prices and limiting the accessibility to consumers of vision care products and services. Under this proposal, the FTC states as follows:

"One category of restriction under review inhibits the commercial or high volume practice of optometry and opticianry. (Optometry is the examining of eyes and the prescribing of corrective lenses and opticianry is the dispensing of eyeglasses.) For example, approximately 40 States prohibit optometrists and/or opticians from engaging in one or more of the following practices: working for non-professional corporations or department stores; locating in high-traffic commercial locations such as shopping centers; operating branch offices; and using trade names.

"The second category of restrictions that the FTC staff has examined consists of those prohibiting opticians from (1) duplication, a process whereby a new eyeglass lens is produced by analyzing the prescription of an existing lens, and (2) fitting of contact lenses. These restrictions may limit the consumer's ability to comparison shop for eyeglasses or contact lenses, particularly when consumers are not given a copy of the prescriptions following the initial sale of eyeglasses or contact lenses. The Commission's Eyeglasses Rule currently mandates prescription release only after the eye examination and not after the dispensing of prescription lenses."

The Eyeglasses Rule was based exclusively on the FTC's unfairness authority. It was predicated upon the premise that it was basically unfair to place a ban on the advertising of products because such a ban cuts off the free flow of information. Deception wasn't a basis at all for the rule. The same thing was true with the eyeglass prescription issue. The Commission determined that it was basically unfair to deny a customer a copy of an eyeglass prescription or to charge an extra charge for such prescription. Deception, again, was not involved.

D. Prescription price advertising issue

During 1975, the FTC began a study of prescription price advertising. Our Associations presented a six-page letter with exhibits which outlined the problem of drug price disclosure and offered suggested solutions. We also responded to an FTC request for a selection of letters we received from our members concerning their high drug expenditures. Subsequently, the FTC announced promulgation of a proposed trade rule which would remove all state bans on prescription price advertising as being in restraint of trade and contrary to the public interest. Our Associations contributed heavily to the FTC Staff Report which was issued to support the rule action. We were especially concerned with issues relating to mail service pharmacies and opposition which had been raised against them by state boards of pharmacy and professional pharmacist organizations.

In December 1975, the FTC held hearings on the proposed trade rule in Chicago, San Francisco and Washington, D.C. Witnesses representing our two organizations testified at each location.

In addition to our comments and testimony before the FTC, the Associations engaged in an extensive educational effort to make our members aware of the purpose and intent of the proposed rule. As a result of this educational effort, the FTC received a good deal of mail from our members in support of the agency's action.

In May 1976 the Supreme Court handed down a decision in the *Virginia Citizens Consumer Council* v. *State Board of Pharmacy* which overturned all state laws and regulations which prohibit prescription price advertising.

FTC's consideration of the prescription price advertising issue was based upon the unfairness authority. The main issue was whether the failure to give material information was unfair.

III. THE PROFESSIONS

A. Health care costs background

Health care cost containment is a matter of great concern to our nation's elderly. Recent surveys of our Associations' membership have clearly indicated that inflation is the number one concern of older Americans. In fact, nearly 80 percent of our volunteer leaders have voiced strong preference for legislation specifically designed to curb inflation over legislation designed to expand benefits to offset the effects of inflation. Within this context perhaps the greatest outpouring of support has been for immediate and effective legislative remedies to deal with rapidly escalating health care costs and to develop some semblance of price competition in the health care marketplace. Given the federal government's role as a massive purchaser of health care services, our Associations feel that efforts toward a more responsible fiscal policy and balanced budget must incorporate strong and effective legislation aimed at this unique sector of our economy. We strongly believe that, without immediate and effective legislative remedies to contain spiraling health care costs, we will be facing proposals for large cuts in our public health insurance programs and needed, meaningful benefits expansion in these programs will be impossible to achieve.

The burden of health care cost inflation falls disproportionately upon the elderly who—while accounting for 11.2 percent of our population—represent 29 percent of our nation's total health care expenditures. Since older Americans in failing health utilize the health care system to a greater extent, the availability, affordability and accessibility of quality health care services is especially important to this segment of our population. While longer life has truly been one of our society's most conspicuous achievements, when combined with declining birth rates, this accomplishment inevitably leads to a rapid growth in the number of older Americans and a greatly increased demand upon our health care delivery system. By the year 2025, the portion of our total population over the age of 65 will increase from 11.2 percent (1980) to 17.2 percent (or 50 million people).

The costs of health care are sharply increasing, adding to the general rate of inflation and threatening the stability of government budgets. The nation's health spending is projected to increase from $287 billion in 1980 to approximately $393 billion in 1984—up from 9.4 to 10.2 percent of our Gross National Product (GNP), for these years. In 1980, alone, health care spending jumped from 8.9 percent to 9.4 percent of the U.S. economy's output (GNP), the fastest growth rate in 15 years. Federal health care expenditures (tied as they are to increases in the price of health care services), if unchecked, will also continue to escalate from $62.4 billion in fiscal year 1981 to over $110 billion by fiscal year 1984—or more than 15 cents out of every Federal tax dollar for that year (under current law projections and without hospital cost containment legislation). For individual health care needs, costs will also rise precipitously. Without strong and effective cost containment measures, the average annual health care costs of a family of four will jump from $2,373 in 1979 to $4,064 in 1984. During the same time period, the cost for a single aged person will rise from $2,259 to $3,868 per year.

The per capita health bill for persons 65 and over was approximately 2½ times that for persons under the age of 65 in 1979. While Medicare was designed to pay 80 percent of the elderly's hospital and physician costs, in 1977 it covered only 73 percent of the former and only 55 percent of the latter. The results of this, plus escalating costs for other needed services, such as nursing home care, drugs, dental care and eyeglasses (which are uncovered or inadequately covered), are that older Americans are spending more out-of-pocket for health care today than they did before the inception of Medicare and the Medicare is presently covering only 38 percent of the elderly's total health care bill (when beneficiary deductibles, insurance premiums and cost sharing are considered). A full 35 percent of the average health bill of an older American is now paid for out-of-pocket. This figure can be expected to rise based on recent large increases in the Part A and Part B deductibles as passed in the fiscal year 1982 budget reconciliation bill. Only 6 percent of per capita expenditures are covered by private health insurance. Clearly, increasing health care costs and diminishing benefits are constricting the elderly's access to needed health services.

Also, recent CPI figures are equally alarming and instructive—showing an accelerated upward trend in the cost of medical care services. From July to August 1981, the cost of hospital and other medical services rose 2 percent (24 percent annualized and nonadjusted) and medical care services were up 1.3 percent (15.6 percent annualized and nonadjusted). Whatever previous success the Voluntary Effort claimed in holding the line on increasing hospital and physical costs now appears to have evaporated. There is clearly a desperate need to implement cost containing measures in this highly inflationary segment of our economy.

B. The associations' position

Against this background, the Associations have long supported the FTC in its efforts to police restraint of trade against professionals. It is our belief that competition is the best way to keep down rapidly escalating costs of health care, and that the FTC's efforts to curb such things as price fixing and boycotts have been efforts toward promoting competition. In addition, we feel the FTC's activities have been consistent with the Congressional and Administration goals of promoting competition and eliminating unnecessarily burdensome regulation. We, therefore, wish to see the professions remain under the jurisdication of FTC.

We strongly feel that any effort to remove the professions from FTC jurisdiction is not in the public interest. Such a special exemption simply suggests that certain persons are beyond the rules by which other members of our society are governed. It is our belief that if professionals are free to enforce restrictions that result in barriers to free consumer choice and artificially inflated prices, immune from the safeguards of the FTC Act, the evidence is strong that consumers will suffer direct and tangible injury.

C. The FTC's position

All of the sitting members of the FTC oppose a special exemption for the professions. Chairman Miller, speaking on behalf of the Commission, has stated:

"I see no basis of principle upon which one or another industry can argue that its anti-competitive, unfair, or deceptive conduct is entitled to special exemption from the law . . . I don't believe the FTC can effectively accomplish its mission if such a significant sector of our economy is, by definition in law, immunized, sanctified, and set aside as a privileged class."

Therefore, the FTC is strongly and unalterably opposed to any amendment to exempt professionals from FTC enforcement of the antitrust and consumer protection laws of this country. We commend them for this strong stance.

The FTC sums up its activities with regard to the professions as follows:

"The Federal Trade Commission has, over the last several years, examined certain practices of professionals and their organizations. Our activities do not derive from any desire to regulate the professions but rather from a basic concern that some restrictions on competition among professionals increase consumer costs without producing countervailing benefits. Our objective, in both our competition and our consumer protection activities, is to enhance the ability of informed consumers to act as ultimate regulators of the market.

"Professional services are an increasingly important sector of the economy, and the efficiency of this industry is of prime importance to consumers. The service sector has been the most rapidly growing component of the economy for many years. (*Health care,* the major focus of recent Commission interest, is the largest single component of the service sector. In 1980 alone, Americans spent over $247 billion on health care services or 9.4 percent of the Gross National Product.)

"In light of these facts, the Commission believes that effective consumer protection and the fostering of competition cannot exclude professional services. The Commission's activities in this area have not sought to interfere either with legitimate self-regulation or with the authority of the states to assure the quality of services to their citizens. Instead, the record shows that the Commission has concerned itself only with specific barriers to competition and restrictions that demonstrably harm consumers."

In addition, OMB Director David Stockman, speaking on behalf of the Administration, voiced opposition to a special exemption for professions on April 1, 1982. He stated the Administration opposed "blanket immunity to the professions" and saw "no cause to exempt" any special group from FTC jurisdiction.

D. FTC and the professions

(1) Antitrust Cases.

FTC antitrust cases have involved activities of three general types:

(1) Alleged agreements to restrict the flow of truthful information about professional services.

(2) Alleged agreements to impede market entry by innovative forms of practice, such as salaried physicians or prepaid medical plans.

(3) Alleged agreements to prevent, by organized boycotts, insurers' use of cost containment programs.

These cases date back 39 years to 1943 when the Supreme Court affirmed the American Medical Association's conviction for violating the Sherman Act. Throughout this history, FTC antitrust cases have been directed at illegal private conduct and have challenged private agreements which eliminate competition in the business and financial aspects of professional practice. It has never challenged state regulation of professions. Nor, has it sought to stop legitimate self-regulatory activities of professional groups.

FTC antitrust cases have challenged the following types of conduct:

Doctors' agreement to boycott Medicaid patients in order to coerce Michigan Medicaid agency to increase fees paid to doctors.

Illegal threats by a small town's only doctors to boycott the local hospital's emergency room patients if the hospital persisted in plans to recruit a new physician competitor to practice at the hospital.

Ethics prohibition physicians working below "usual" rates or for "inadequate" compensation use by American Medical Association in attempt to fix price levels and prevent hospital and health maintenance organizations from reducing costs by hiring salaried physicians and passing savings on to consumers.

Conspiracies in Pennsylvania, Washington, and other states to boycott physicians who work on a salary for innovative, low-cost health maintenance organizations, by excluding these doctors from hospitals, participation in Blue Shield, local medical associations, and malpractice insurance coverage.

Sweeping advertising and customer solicitation bans denying consumers access to truthful information on medical and dental prices and services, used by professional associations to, for example, block a church organization from operating and publicizing a low-cost cardiac stress clinic, to help drive a physician house-call service in Kansas out of business, to stop a physician specialist from offering an industrial medicine program to corporations for their workers, and to prevent senior citizens from learning which doctors receive Medicare payments.

Conspiracy by doctors to obstruct a union- and employer-developed cost-containment program for auto industry workers and force fee level increases by collectively refusing to participate in a state Blue Cross-Blue Shield plan.

Unlawful prohibition by American Medical Association on physicians forming business partnerships or income-sharing arrangements with licensed non-physician professionals, such as clinical psychologists.

Conspiracy of dentists to refuse cooperation with dental insurance plans' cost-containment programs.

(2) FTC actions have stopped fraudulent behavior by professionals.

For example, the FTC has challenged:

Undisclosed health risks involved in a doctor's synthetic hair implant business.

Deceptive advertising by a weight clinic that use a prescription drug never approved by the FDA as safe and effective for treatment of obesity.

(3) The FTC has proceeded cautiously in examining whether and when professional regulation imposes substantial costs on consumers without providing any countervailing benefits.

Studies show that some restrictions on the business aspects of professional practice do not increase quality but do increase prices, restrict choices, and reduce availability of professional goods and services. For example:

Higher prescription drug prices resulted from state laws restricting price advertising. A 1975 study estimated that these regulations cost consumers $134 million in one year.

Higher prices for eyeglasses exist in states with regulations strictly limiting competition among optometrists. A 1975 study estimated that these regulations increased eyeglasses prices by 34 percent.

More expensive optometric services, as well as higher priced eyeglasses, result from regulations preventing certain business practices. A 1979 FTC study found some regulations increased prices by 17 percent without increasing the quality of care.

Needed services are not obtained when prices increase. Studies of optometry, dentistry, and law show that higher prices mean that consumers do not obtain necessary services.

It should be noted that FTC studies on the effects of regulations have been designed and conducted with assistance of members of the affected professions. In addition, the Eyeglasses Rule, which is discussed at length beginning on page 20 of this testimony, is the one rule the FTC as issued that directly addressed restrictions on competitive behavior of professionals.

Since all of the aforementioned FTC activities with regard to professionals involve health-related issues, we, naturally, continue to support the efforts of the FTC on this area. It is our belief that these activities have helped to keep down the rising costs of health care through promoting competition. Therefore, we strongly oppose the elimination of professionals from FTC jurisdiction.

E. Definition of professionals

While several proposals have been tossed around, there is a great deal of confusion as to just what a professional is. You can well imagine the confusion that would be created if an exemption for professions were enacted. This confusion would come about as the result of everyone clamoring to make sure his or her group was included in the definition. One of the sponsors of S. 1984 has stated that the term includes "lawyers, engineers, physicians, dentists, optometrists, architects, accountants, veterinarians, *and the like.*" What about bartenders, paralegals, hairdressers, barbers, people in the building trades (bricklayers, electricians, carpenters, plumbers, etc.) bankers, teachers, chefs, bakers, insurance agents, real estate agents, college professors, etc.? Just where would the line be drawn to delineate between the professional and non-professional? Given the imprecise nature of the definition of profession, virtually *any* occupation would probably be able to argue that it too was exempt from FTC authority. In addition to the pressure that would be placed upon the Congress to include certain groups in the "profession" definition, the courts would also be deluged with cases attempting to define the term.

It has been estimated by some observers that on average, over one hundred occupations are currently licensed within each state and might possibly be considered "professions." In light of this, and exemption for professions would remove billions of dollars of interstate commerce and much of the service sector of our economy from the FTC's law enforcement and deregulatory efforts. This, we find, would be totally unacceptable.

It is the Associations' position that the professions need to remain under FTC jurisdiction and that any effort to elevate them to a "special status" immune from FTC recourse would simply be opening up a can of worms.

IV. REAUTHORIZATION FUNDING

The present authorization for fiscal year 1982 is $80 million, compared to a proposed appropriation for fiscal year 1983 of $60.8 million. The Associations support a continued authorization level of $80 million for the next three years with the Appropriations Committees determining how much of this is available in the budget.

CONCLUSION

In closing, we would like to reiterate our positions on the major issues facing the FTC at the present time. They are: (1) the law of deception, as it currently exists, should remain intact and should not, in any way, be altered; (2) the FTC should retain its unfairness authority without a statutory definition; (3) the professions should not be exempted from FTC authority; and (4) the current funding level should be maintained.

The FTC has been very instrumental in protecting the interests of the elderly in numerous ways. If the aforementioned suggestions are followed, we feel the FTC will be able to continue to protect the rights of the elderly in the future.

STATEMENT OF SUNKIST GROWERS, INC.

INTRODUCTION

Sunkist Growers, Inc., is a nonstock, nonprofit agricultural marketing cooperative organized under the California Food and Agriculture Code, Division 20, Chapter 1. Its membership consists of approximately 6,500 citrus growers in Arizona and California. Most are family farmers who farm an average of 35 acres of citrus. They produce oranges, lemons, grapefruit, tangerines, and limes.

As the sales agent for its grower-members, Sunkist has established sales offices throughout the United States and Canada, and has utilized sales agents abroad. Grower-members also turn to the cooperate to help process the citrus they cannot sell in the fresh market. Sunkist provides additional marketing assistance through its export marketing, transportation, and researh development functions.

This statement is being submitted for the record on behalf of Sunkist in support of the continuation of Section 20 of the Federal Trade Commission Reauthorization of 1980, P.L. 96-252. Section 20 prohibits the Federal Trade Commission (FTC) from "conducting any study, investigation, or prosecution of any agricultural cooperative for any conduct [which is not in violation of the Capper-Volstead Act of 1922, 7 U.S.C. 291 *et seq.*]," and from "conducting any study or investigation of any agricultural marketing orders." It is our belief that on both statutory and fiscal grounds, this section should be preserved.

THE CAPPER-VOLSTEAD ACT ESTABLISHES THAT PRIMARY JURISDICTION OVER COOPERATIVES RESTS WITH THE SECRETARY OF AGRICULTURE

Special antitrust treatment for agricultural dates back to the Clayton Act of 1914, 15 U.S.C. §12 et seq., when the modern cooperative movement was beginning to emerge. Section 6 of that Act, 15 U.S.C. §17, established a narrow antitrust exemption for cooperatives organized without capital stock. As cooperatives increased in popularity, farmers recognized the need for a broader and more explicit antitrust exemption for cooperative activity. Accordingly, in 1922, they sought and obtained the Capper-Volstead Act, which specifically authorized the formation of agricultural cooperatives, granted an antitrust exemption, and vested initial jurisdiction over cooperative activity with the Secretary of Agriculture.

Section 1 of the Capper-Volstead Act, 7 U.S.C. §291, provides that producers of agricultural products may—

". . . act together in associations, corporate or otherwise, with or without capital stock, in collectively processing, preparing for market, handling, and marketing in interstate and foreign commerce, such products or persons so engaged. Such associations may have marketing agencies in common; and such associations and their members may make the necessary contracts and agreements to effect such purposes:

Provided, however, That such associations are operated for the mutual benefit of the members thereof . . ."

Section 2 of the Act, 7 U.S.C. §292, relates to jurisdiction over agricultural cooperatives and states that—

"[i]f the Secretary of Agriculture shall have reason to believe that any such associaton monopolizes or restrains trade in interstate or foreign commerce to such an extent that the price of any agricultural product is unduly enhanced by reason thereof, he shall serve upon such association a complaint . . . [and] a notice of hearing . . . If upon such hearing the Secretary of Agriculture shall be of the opinion that such association monopolizes or restrains trade in interstate or foreign commerce to such an extent that the price of any agricultural product is unduly enhanced thereby, he shall issue . . . an order . . . directing such association to cease and desist . . ."

The legislative history of the Capper-Volstead Act makes clear that the drafters intended to vest the Secretary of Agriculture with primary jurisdiction, as they specifically rejected conferring such jurisdiction to the Federal Trade Commission. When the legislation was first proposed, the House version vested initial jurisdiction in the Secretary of Agriculture; the Senate Judiciary Committee version vested this jurisdiction in the FTC.[1] On the Senate Floor, an amendment to the House version was offered which substituted the words "Federal Trade Commission" for the words "Secretary of Agriculture" wherever they appeared. With this language before it, the Senate voted "No" on the precise issue of the FTC initial jurisidiction over Capper-Volstead cooperatives.

Thus, Congress determined that the Department of Agriculture could better analyze cooperatives to ascertain whether or not they had stepped beyond the permissible bounds of the statute. Its determination is reflected not only in the legislative history, but also on the face of the statute. To give meaning to his statutory intent, Section 20 of the Federal Trade Commission Reauthorization of 1980 should be continued.

THE EVOLUTION OF FEDERAL MARKETING ORDERS FOR FRUITS AND VEGETABLES

Because of the severely depressed conditions of farmers during the 1930's resulting in chaotic volume and price swings for agricultural commodities, Congress enacted the Agricultural Adjustment Act of 1933, which was reenacted and amended by the Agriculture Marketing Agreement Act of 1937. 7 U.S.C. § 601. This legislation authorized the Secretary to enter into "marketing agreements" with producers, processors and handlers of any agricultural commodity and excluded the making of these agreements from the application of antitrust laws. 7 U.S.C. § 608b. In addition, the Secretary of Agriculture was authorized to enter "marketing orders" to control the flow of designated agricultural commodities to markets. 7 U.S.C. § 608c.

At the present time, there are 47 federal marketing orders for fresh fruits and vegetables, each administered by an administrative committee comprised of producers, growers, handlers and public members. These orders may empower marketing committees to provide for marketing and research projects, require inspection of the subject commodity, establish grade and size requirements and regulate the container in which the commodity is shipped. In addition, the orders may authorize marketing committees to restrict the quantity of the commodity to be handled, control surpluses, and establish reserve pools.

The responsibility for monitoring and enforcing these marketing orders is placed with the Secretary of Agriculture. Since 1937, the Department of Agriculture has worked to develop the expertise necessary to carry out this responsibility. It routinely investigates the costs and benefits to the producer and consumer of marketing orders to ensure that these orders serve their statutory purpose. One such investigation was recently completed by the Department of Agriculture at the request of the Vice President's Task Force on Regulatory Reform. The final report recommended minor changes in some orders, but concluded that marketing orders were generally serving their statutory function and did not appear to unduly enhance prices.

Because marketing orders are adequately monitored and enforced by the Department of Agriculture as authorized by the Agricultural Marketing Agreement Act of 1937, there is no need for the FTC to duplicate such efforts. The Department of Agriculture, not the FTC, has the statutory authority and the requisite experience to accomplish these responsibilities.

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[1] See Attachment A containing comments of Senator Kellog, floor manager in the Senate debate, urging his colleagues to accept the House version and not the Senate Committee version on this point. Note in particular, his opening phrase regarding the purpose of designating the Secretary of Agriculture as the person most competent to deal with these questions. See also Attachment B containing opposing comments of Senator King who wanted the FTC to have jurisdiction.

THE FEDERAL TRADE COMMISSION'S INVESTIGATIONS OF AGRICULTURAL COOPERATIVES AND MARKETING ORDERS ARE DUPLICATIVE AND COSTLY

Even though the Secretary of Agriculture is vested by statute with the authority for primary jurisdiction over agricultural cooperatives and marketing orders, the Federal Trade Commission has persisted in investigating these areas for undue price enhancement and unfair trade practices.

In 1975, the FTC requested voluminous amounts of information from the fifty largest agricultural cooperatives as part of a study on the role of agricultural cooperatives in certain sectors of the economy. The cooperatives were instructed to submit within 30 days detailed financial and membership information as well as speeches, press releases, and other materials prepared during a three year period. Failure to comply meant a penalty of $100 per day.

As a result of the Federal Trade Commission's general investigation of agricultural cooperatives, complaints were filed against Sunkist Growers, Inc. In defending itself from the FTC complaint, Sunkist incurred expenses of approximately $1 million a year, which represented approximately 6 percent of its operating budget. An assessment was imposed on each member grower to cover that expenditure. Faced with these costs, Sunkist was forced to enter into a consent decree in 1980 to settle the case.

SECTION 20 OF THE 1980 FEDERAL TRADE COMMISSION REAUTHORIZATION

As a result of the Federal Trade Commission's duplicative and costly investigations against agricultural cooperatives and marketing orders, an amendment to the FTC's reauthorization legislation was introduced in 1980, prohibiting the Commission from expending any funds to investigate, study or monitor agricultural cooperatives or marketing orders. The purpose of the amendment was to stop the abuse of authority by the FTC in violation of the Capper-Volstead Act.

As finally adopted, the amendment provided the following:

"Section 20(a) The Federal Trade Commission shall not have any authority to use any funds which are authorized to be appropriated to carry out the Federal Trade Commission Act (15 U.S.C. 41 et seq.) for fiscal year 1980, 1981 or 1982 . . . for the purpose of conducting any study, investigation or prosecution of any agricultural cooperative for any conduct which, because of the provisions of the Act . . . commonly known as the Capper-Volstead Act is not a violation of any federal antitrust act or the Federal Trade Commission Act.

"(b) The Federal Trade Commission shall not have any authority to use any funds which are authorized to be appropriated to carry out the Federal Trade Commission Act for fiscal year 1980, 1981, or 1982 . . . for the purpose of conducting any study or investigation of any marketing orders."

The President signed the FTC reauthorization bill in June, 1980.

CONCLUSION

The Capper-Volstead Act of 1922 gives express authority for primary jurisdiction over agricultral cooperatives to the Secretary of Agriculture. Under the Agricultural Marketing Agreement Act of 1937, the Secretary has also been vested with the authority to monitor and enforce marketing orders. Accordingly, the Department of Agriculture has supervised both Capper-Volstead cooperatives and agricultural marketing orders for the past fifty years. During this time, the Department has developed a unique expertise in this complex area and has established complete competency.

To prevent the Federal Trade Commission's unwarranted investigations into agricultural cooperatives and marketing orders, the Congress in 1980 prohibited the Commission from any further action in that area through fiscal year 1982. Since that time, the Department of Agriculture has completed a comprehensive review of agricultural marketing orders at the request of the Vice President's Task Force on Regulatory Reform. In addition, the Department of Agriculture recently issued detailed regulations for reviewing complaints under Section 2 of the Capper-Volstead Act. 7 C.F.R. § 1.60 et seq.

Thus, in compliance with established law, the Department of Agriculture has established the expertise to thoroughly and objectively monitor Capper-Volstead cooperatives and marketing orders. During this time of high budget deficits, the Federal Trade Commission must not be permitted to use its funds for the purpose of duplicating such efforts. Accordingly, Sunkist strongly supports preserving the prohibition langauge of Section 20.

SENATOR KELLOGG'S STATEMENT

Senator Kellogg, Floor Manager of the House version, asked the Senate to pass the bill as it came from the House, without the Senate Judiciary Committee amendment. Commenting upon the House version he said that the first question raised is why the Secretary of Agriculture should have sole administrative jurisdiction to determine if there are monopolies or restraints of trade. He explained:

"I know of no officer more competent to deal with that question than the Secretary of Agriculture. He has in his department a Bureau of Markets. He keeps track of the cost of production, the cost of selling, and what the public is paying. He has the statistics and he, through his Bureau of Markets, can determine better than any other agency of the Government whether such a cooperative marketing association is really being operated in restraint of trade as a monopoly and is unduly enhancing prices.

"The Attorney General has the duty placed upon him to take charge of the suit in the court and to prosecute it, but the Attorney General has not the machinery to study these cooperative associations, to find out the cost of production, the cost of selling, the reasonable prices to the consumers, and various other elements which it is easy for the Secretary of Agriculture to find out.

"It may be said, therefore, that before such associations can be prosecuted under the Sherman Act for any restraint of trade or monopoly, whether it is a mere technical monopoly or not, the Secretary of Agriculture must investigate and make a finding that the cooperative association is in restraint of trade or is a monopoly and is unduly enhancing prices."

SENATOR KING'S OPPOSING ARGUMENTS

Senator King, an opponent of the House version who was distressed that the House version would preclude FTC jurisdiction, phrased the issue as follows:

"Undoubtedly the purpose back of the creation of the Federal Trade Commission was commendable. The Federal Trade Commission has machinery far greater than that possessed by the Secretary of Agriculture for the performance of the work which this bill seeks to impose upon the Secretary of Agriculture. I am very earnest in my appeal to the Senate to consider the unwisdom, the incongruity of conferring upon the head of a department quasi-legislative functions.

"We have set up in the Government the Federal Trade Commission for the purpose of investigating evils and unfair practices and for the purpose of seeing that justice is done between producers and, indeed, in one sense between producers and consumers.

"The law provides that when the commission have reason to believe that a partnership, corporation, or, person has been using any unfair method of competition in trade or commerce, they shall proceed to make an investigation. . . . They have the machinery, investigators, and lawyers for the purpose of investigating into such matters as would come within the authority of the Secretary of Agriculture under the provisions of this bill.

"The Senator says that the Secretary of Agriculture has the reports of the Market Division or Bureau. If those reports are of any value whatever . . . the Federal Trade Commission would have access to those reports, and they could ascertain their contents just as easily as the Secretary of Agriculture could. . . .

"It does seem to me that if we depart from the principle which was announced in the Federal Trade Commission act, and commit to a department investigations of the character provided in this bill, and the determinations of the questions which call for determination in this bill, we are establishing a very unwise precedent."

62 Cong. Rec. 2278-79 (1922).

STATEMENT OF THE CALIFORNIA ALMOND GROWERS EXCHANGE

INTRODUCTION

The California Almond Growers Exchange is an agricultural cooperative located in Sacramento, California. The Exchange has 5,000 member-growers, or approximately 72 percent of the almond growers in California.

The Exchange receives, processes, packs and markets almonds for its members; its almond supply is obtained exclusively from its members. The Exchange sells the almonds of its members throughout the United States and in nearly every country of the world.

There are currently 365,000 bearing and nonbearing acres of almond trees in California, making almonds the largest tree crop in the state. A projected 100,000 additional acres are to be planted. The total fiscal year 1980 sales of almonds amounted to approximately $700 million.

This statement is being submitted for the record on behalf of the California Almond Growers Exchange in support of the continuation of Section 20 of the Federal Trade Commission Reauthorization of 1980, P.L. 96-252. Section 20 prohibits the Federal Trade Commission (FTC) from "conducting any study, investigation, or prosecution of any agricultural cooperative for any conduct [which is not in violation of the Capper-Volstead Act of 19722, 7 U.S.C. 291 et seq.]," and from "conducting any study or investigation of any agricultural marketing orders." It is our belief that on both statutory and fiscal grounds, this section should be preserved.

THE LEGISLATIVE HISTORY OF THE CAPPER-VOLSTEAD ACT ESTABLISHES THAT PRIMARY JURISDICTION OVER COOPERATIVES RESTS WITH THE SECRETARY OF AGRICULTURE

Special antitrust treatment for agriculture began in the early 1900's with the passage of the Clayton Act of 1914, 15 U.S.C. § 12 et seq., which recognized the need for small farmers to form cooperative associations in order to compete with large corporations. Section 6 of that Act, 15 U.S.C. § 17, established a limited antitrust exemption for cooperatives organized without capital stock. With the increasing popularity of the cooperative movement, it became clear that the exemption provided by the Clayton Act would not prevent prosecution for conspiracy in restraint of trade. Accordingly, in 1922, they sought and obtained the Capper-Volstead Act, which specifically authorizes the formation of agricultural cooperatives, grants a limited antitrust exemption, and vests initial jurisdiction over cooperative activities with the Secretary of Agriculture.

When the Capper-Volstead Act was first introduced, the issue of where to place initial jurisdiction over cases involving agricultural cooperatives was debated by Congress in some detail. The House version vested initial jurisdiction in the Secretary of Agriculture; the Senate Judiciary Committee version vested such jurisdiction in the FTC. In the Senate, a floor amendment was offered to the House version substituting the words "Federal Trade Commission" for the words "Secretary of Agriculture" wherever they appeared. The amendment was rejected by the Senate in favor of the language explicitly conferring initial jurisdiction to the Secretary of Agriculture.

As finally enacted, Section 1 of the Capper-Volstead Act, 7 U.S.C. § 291 provides that producers of agricultural products may act together in corporate or non-corporate associations, operated for the mutual benefit of the member producers, "in collectively processing, preparing for market, handling, and marketing" their products in interstate and foreign commerce. The section also authorizes such associations to have marketing agencies in common and to "make the necessary contracts and agreements to affect such purposes."

Section 2 of the Act, 7 U.S.C. § 292, states that if the Secretary of Agriculture believes that any such association, "monopolizes or restrains" interstate trade "to such an extent that the price of any agricultural product is unduly enhanced by reason thereof," the Secretary must serve upon the association a complaint. If, after a hearing, the Secretary finds that there has been such a monopolization or restraint of trade and undue price enhancement, he is required by Section 2 to issue an order directing the association to "cease and desist". This section confers jurisdiction upon the district court to enter a decree enjoining violation of the Secretary's order, or a decree modifying or setting aside the order, and provides that the Department of Justice shall have charge of the enforcement proceeding.

In sum, the purpose of the Capper-Volstead Act was to protect farmers by allowing them to form associations for their mutual benefit without antitrust interference. Congress determined that the Department of Agriculture could better analyze cooperatives to ascertain whether or not they had stepped beyond the permissable bounds of the statute. This determination is reflected not only in the legislative history, but also on the face of the statute.

THE EVOLUTION OF FEDERAL MARKETING ORDERS FOR FRUITS AND VEGETABLES

Because of chaotic volume and price swings for agricultural commodities during the Depression, Congress enacted the Agricultural Adjustment Act of 1933, which was later incorporated into the Agricultural Marketing Agreement Act of 1937. 7 U.S.C. § 601 et seq. This legislation authorized the Secretary to enter into marketing agreements "with producers, processors and handlers of any agricultural commodity and excluded the making of these agreements from the application of antitrust laws." 7 U.S.C. § 608b. In addition, the Secretary of Agriculture was authorized to enter "marketing orders" to control the flow of designated agricultural commodities to market. 7 U.S.C. § 608c.

There are currently 47 federal marketing orders for fresh fruits and vegetables established under the Agricultural Adjustment Act. Each is administered by an administrative committee comprised of producers, growers, handlers and public members. These committees may be authorized to provide for marketing and research projects, require inspection of the commodity, establish grade and size requirements and regulate the container in which the commodity is shipped. The marketing committees may also have the power to restrict the quantity of the commodity to be handled in any period, control surpluses, and establish reserve pools.

The Secretary of Agriculture has the ultimate responsibility for monitoring and enforcing these marketing orders. Over a period of 45 years, the Department of Agriculture has worked to develop the expertise necessary to carry out this responsibility by routinely investigating the costs and benefits to the producer and consumer of marketing orders. The most recent of these investigations was just completed by the Department of Agriculture at the request of the Vice President's Task Force on Regulatory Reform. The final report recommended minor changes in some orders, but concluded that marketing orders were generally serving their statutory function and did not appear to unduly enhance prices.

The Department of Agriculture has the statutory authority and the requisite experience necessary to monitor these marketing orders. The FTC shoud not attempt to duplicate these efforts.

THE FEDERAL TRADE COMMISSION'S INVESTIGATIONS OF AGRICULTURAL COOPERATIVES AND MARKETING ORDERS ARE DUPLICATIVE AND COSTLY

Although the Secretary of Agriculture is statutorily vested with the authority for primary jurisdiction over agricultural cooperatives and marketing orders, the Federal Trade Commission has nevertheless persisted in investigating these areas for undue price enhancement and unfair trade practices.

In 1975, the FTC requested considerable quantities of information from the fifty largest agricultural cooperatives to study the role of agricultural cooperatives in certain sectors of the economy. The cooperatives were instructed to submit within 30 days detailed financial and membership information as well as speeches, press releases, and other materials prepared during the previous three years. Failure to comply would result in a penalty of $100 per day.

As a result of the Federal Trade Commission's general investigation of agricultural cooperatives, complaints were subsequently filed against the Central California Lettuce Producers Cooperative alleging price-fixing. Charges alleging unfair trade practices were also brought against Sunkist Growers, Inc. After initiating the Sunkist investigation the FTC announced it would also investigate Ocean Spray, Inc.

In August, 1977, the FTC dismissed by unanimous vote the complaint against Central California Lettuce, but only after cooperative had incurred enormous costs in defending the complaint. Sunkist, too, suffered great costs participating in protracted discovery proceedings and was forced to enter into a consent decree to settle the case. The FTC investigation of Ocean Spray, Inc. did not materialize.

THE SECTION 20 PROHIBITION OF THE 1980 FEDERAL TRADE COMMISSION REAUTHORIZATION

As a result of the Federal Trade Commission's repeated investigations and complaints filed against agricultural cooperatives and marketing orders, an amendment was introduced to the 1980 FTC reauthorization legislation prohibiting the Commission from expending any funds to investigate, study or monitor agricultural cooperatives or marketing orders. The intent of the legislation was to stop the abuse of authority by the FTC in violation of the Capper-Volstead Act. The Section 20 prohibition expires on September 30, 1982.

CONCLUSION

The Capper-Volstead Act of 1922 gives express authority for primary jurisdiction over agricultural cooperatives to the Secretary of Agriculture. The Secretary has also been vested with the authority to monitor and enforce marketing orders under the Agricultural Marketing Agreements Act. In compliance with these laws, the Department of Agriculture has monitored Capper-Volstead cooperatives and agricultural marketing orders for the past fifty years. During this time, the Department of Agriculture has developed a unique expertise in this complex area and has established complete competency.

To curb the Federal Trade Commission's unwarranted investigations into agricultural cooperatives and marketing orders, the Congress in 1980 prohibited the Commission from any further action in that area through fiscal year 1982. Since that time, the Department of Agriculture has completed a comprehensive review of agricultural marketing orders at the request of the Vice President's Task Force on Regulatory Reform. The Department of Agriculture has also issued detailed rules of practice governing "cease and desist" proceedings under Section 2 of the Capper-Volstead Act. 7 C.F.R. §1.160 et seq.

There is no need for the Federal Trade Commission to duplicate the Department of Agriculture's investigations of agriculture cooperatives or marketing orders. The Department of Agriculture is fully capable of satisfying its statutory responsibilities. In addition, the Justice Department retains jurisdiction to file antitrust actions under the Sherman or Clayton Acts. This jurisdiction includes actions relating to pre-merger notifications filed by cooperatives under the Hart-Scott-Rodino Act, 15 U.S.C. §18a, an area over which the Department of Justice has capably exercised its authority. Individual states' Attorneys General are also free to file antitrust complaints, and private parties may file antitrust suits against agricutural cooperatives. Given our high federal deficits, duplicative efforts by the FTC should not be permitted.

For the foregoing reasons, the California Almond Growers Exchange fully supports the continuation of Section 20 and urges this Committee to retain the prohibition language.

STATEMENT OF AMERICAN ACADEMY OF OPHTHALMOLOGY

The American Academy of Ophthalmology is the largest non-profit medical ophthalmological organization in the nation. Effective July 1, 1981, the second largest ophthalmological association, the American Association of Ophthalmology, was merged into the Academy bringing its membership of physicians (M.D.s) specializing in medical eye care, (ophthalmology) to more than 11,000. The Academy and its Board of Directors have an advisory Board of Councillors, composed of representatives of ophthalmological organizations from all 50 states, Puerto Rico and the District of Columbia and other specialty associations within ophthalmology. The Academy and its Councillors foster scientific inquiry into the definitive diagnosis, care and treatment of diseases, disorders and injuries to the human eye and the correction of vision deficiencies. The Academy promulgates educational information to the profession, to the public and to government concerning the preservation, improvement and restoration of vision. The Academy exists for the advancement of quality medical eye care, is universally recognized and has had a long standing role in promoting and enhancing the highest level of medical eye care and vision care available in the world. All of its member physicians are examined for competence, are licensed, and are mandated and disciplined under state laws controlling the practice of the healing art, regulated under the police power of the states in the protection of the public health of the people in each state. The states and their licensed physicians are qualified to better monitor and regulate the learned profession of medicine that an appointed federal commission, experienced until quite recently, in attempting to regulate the unfair competition in the marketplace of trade and commerce.

Accordingly, the Academy has reviewed S. 1984 and supports this legislation as necessary to correct arbitrary extentions of power by the Federal Trade Commission (FTC) contrary to its history and to the will of Congress.

REASONS FOR SUPPORT OF S. 1984

S. 1984 removes the illegal intrusion by the FTC into licensed health service areas over which the commission has no jurisdiction

The provision of health care like the practice of the healing art, traditionally is within the jurisdiction of the states. Under the reserved police power to protect the public health, it is the duty of the states to enact licensing laws and regulations in this field authorizing practitioners, such as physicians, to practice the healing art under circumstances and conditions which satisfy the local needs of the states. Not only is the licensing and regulation of the practice of medicine an appropriate exercise of the states, it is one which has benefited the public. Under this system of state regulation medicine has advanced to the stage where medical care in this nation is considered among the best, if not the best in the world.

All states supervise, regulate and license practitioners in the delivery of heatlh care to their residents. These state laws are adopted as regulatory methods, after consideration by state legislatures, to meet local conditions and thereby protect the public health and welfare. The history of state regulation, particularly in the practice of medicine, vindicates the authority of the states to legislate comprehensively in the licensing and regulations of the providers, i.e. doctors of medicine.

The FTC, a five member administrative commission, is neither qualified nor empowered to override and preempt the states regulation of the practice of medicine as mandated by state laws enacted under reserved police power of the states in the public interest.

When the five person Federal Trade Commission was created in 1914, its purpose was to protect against unfair competitive acts by businessmen. No mention was made in its legislative history that the Federal Trade Commission Act gave it jurisdiction over the learned professions of theology, law and medicine. The FTC was given authority to prevent deceptive acts and practices in order to protect consumers and merchants from misleading statements and unscrupulous competitors in the open competition of the marketplace. This authority pertains to commercial enterprises and was never intended to apply to the learned professions. When the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act, a compromise bill, was enacted, the FTC was authorized to adopt trade regulations rules. Neither the act, the House and Senate bills nor the legislative history in the 93rd Congress contained any provision expressly or impliedly giving the FTC any power to preempt state laws in connection with this rulemaking authority. The Senate and House Committee reports articulated the contrary. In explaining the act regarding another provision of the House bill, the House report stated:

"The expansion of the FTC's jurisdiction is not intended to occupy the field or in any way to preempt State or local agencies from carrying out consumer protection or other activities within their jurisdiction which are also within the expanded jurisdiction of the Commission.

"Where cases of consumer fraud of a local nature which affect commerce are being effectively dealt with by state or local agencies, it is the Committee's intent that the Federal Trade Commission should not intrude (H.R. Rep. 93-1107, 93rd Cong., 2d Sess. 45, reprinted in 4 U.S. Code, Cong. and Admin. News 7702, 7726, (1974)."

There is nothing in the conference report of the House and Senate bills indicating that Congress intended to confer on the FTC any power to preempt state laws. Congress in enacting the Magnuson-Moss Act manifested no intention to permit the FTC to strike down valid state licensure laws particularly in the health care field.

Against this background nevertheless, the FTC in enacting Eyeglasses 1 (16 C.F.R. Part 456) in part 9 thereof made clear its intention to invade the states' police powers to regulate health care. This part of the rule reads:

"All state or local laws rules or regulations which burden the dissemination of information by requiring affirmative disclosures specifically addressed to ophthalmic goods and services are pre-empted, except for those specifically permitted by this part."

On petitions to review the FTC's Eyeglasses 1 Rule of the American Medical Association, American Optometric Association and 9 states, in these consolidated appeals, the Court of Appeals for the District of Columbia Circuit held all advertising aspects of the rule did attempt to override state laws and suspended these provisions of the rule. (*American Optometric Association* v. *FTC*, 626 F.2d 896) (D.C. Cir. 1980). In its Advance Notice of Proposed Rule Making in Eyeglases II the FTC has announced an intention to consider promulgating a further prescription rule preempting state laws, rules and regulations in the furnishing of ophthalmic goods and services.

S. 1984 corrects this illegal invasion of the reserved powers of the states by redefining the associations over which the FTC is to have jurisdiction and excepts from FTC jurisdiction: "* * * incorporated or unincorporated association of state regulated professions means non-profit professional associations of practitioners who are independently licensed and regulated by the laws of the respective states." Even the FTC in its letter to the Commissioners of March 5, 1982 concedes: "* * * a more precise standard is appropriate."

The bill further excepts from FTC jurisdiction practitioners of a profession whose members are licensed and regulated by a State as a condition of independent practice within the State, incorporated or unincorporated associations of the State—regulated professions. S. 1984 further provides:

"Nothing in this section shall authorize the Commission to initiate any investigation or proceeding, or promulgate any rule or regulation (excepting rules and regulations already the subject of litigation in the courts) affecting any State regulated profession or individual members thereof or with respect to its State or National professional associations."

S. 1984 also provides that the Commission shall have no authority to prescribe any rule regulating the activity of any person, partnership or corporation which conforms to applicable state law.

History and the law support the reserved right of the states to regulate a learned profession, i.e. the practice of medicine, without federal intrusion

An administrative agency has only such powers granted to it as are enumerated by Congress. In rulemaking it is confined to effecting the will of Congress and the law. Thus in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185, 213–214 (1976) the Supreme Court held:

"The rulemaking power granted to an administrative agency charged with the administration of a federal statute is not the power to make law, rather it is the 'power to adopt regulations to carry into effect the will of Congress as expressed by the statute' ".

Further, the Supreme Court has made it clear that it should never be held that Congress intends to supersede or by its legislation suspend the exercise of the police powers of the states. *Reid* v. *Colorado,* 187 U.S. 137, 148 (1902); *Jones* v. *Rath Packing Company,* 430 U.S. 519, 525 (1977); *Douglas* v. *Sea Coast Products, Inc.* 431 U.S. 265, 272 (1977).

On the question of jurisdiction by the FTC over state licensed medical practitioners, the Academy respectfully points out that the term "trade" as included in the commerce clause of the Constitution and in the federal antitrust laws, including the Federal Trade Commission Act, over the years has been held *not* to include the learned professions of theology, law and medicine. *Schooner Nymph* case (Judge Storey) 18 Fed. Cas. 506, No. 10388, affirming 18 Fed. Cas. 509, No. Fed. 724; *May* v. *Sloan,* 101 U.S. 231; *Federal Club* v. *National League,* 259 U.S. 200; *Toxaway Hotel Co.* v. *Smathers,* 216 U.S. 439, *Holy Trinity Church* v. *United States,* 143 U.S. 457. "Trades" and "Professions" are distinct from each other and involve entirely different considerations. This seems settled law in the Supreme Court since *Dandridge* v. *Washington Executors,* 2 Peter 369. In *Graves* v. *Minnesota,* 272 U.S. 425 p. 429, the Supreme Court held "employment or trades * * * manifestly involved very different considerations than those relating to those professions such as dentistry." Further, in *Federal Trade Commission* v. *Raladam Co.,* 283 U.S. 643, p. 653, the Supreme Court ruled "Medical practitioners * * * follow a profession and not a trade and are not engaged in the business of making or vending remedies but in prescribing them." *In Atlantic Cleaners and Dyers* v. *U.S.,* 286 U.S. 427, page 436, in actually defining "trade" under the Sherman Act the Supreme Court approved the following definition of Judge Storey:

"Whenever any occupation, employment, is carried on for the purpose of profit, or gain or livelihood, not in the liberal arts or in the learned professions, it is constantly called a trade."

Later in *Semler* v. *Dental Examiners,* 294 U.S. 608, page 612, the Supreme Court decided:

"The legislature was not dealing with traders or commodities, but with a vital interest of public health, and with a profession treating bodily ills and demanding different standards of conduct than those which are traditional in the competition of the marketplace."

The police power of the state includes the power to enact comprehensive, detailed and rigid regulations for the practice of medicine, surgery and dentistry. *Douglas* v. *Noble,* 261 U.S. 165 43 S. Ct. 303; *Dent* v. *West Virginia,* 129 U.S. 114, 9 S. Ct. 231; *People* v. *Witte,* 315 Ill. 282, 146 N.E. 178, 37 A.L.R. 672. In *Garcia et al* v. *The Texas State Board of Medical Examiners,* 384 F. Supp. 432, affirmed, 421 U.S. 995, 95 S.Ct. 2391, upholding the Texas Medical Practice Act's prohibition of the corporate practice of medicine, the Court held:

"The right of the State to regulate under its police powers all aspects of the practice of medicine and thereby help provide for the general health and welfare of its citizens is of such vast importance as to approach the status of duty. Nothing is more fundamental than the rights of the various states to furnish the people competent health services and as a direct corollary to this right they have a corresponding duty to carefully prescribe minimum requirements for the licensing of those administering medical and surgical devices. This is a highly specialized field of experts daily dealing with the very lives of the citizenry and the state must, therefore, insure as best it can the competency of these experts.* * * "

In view of this long line of legal authority, the Academy respectfully submits that the investigations made by the FTC under Eyeglasses II and described in Volume 45, No. 237, Federal Register, invade an area reserved to the states over which the FTC has no jurisdiction. Even if the FTC had jurisdiction to adopt rules requiring the release of prescriptions and specifications, which authority the Academy disputes, such prescriptions could mislead and deceive the person receiving them because they cannot be legally utilized under some state laws, as in Texas.

With respect to the FTC's announced intention to rewrite the regulation regarding prescriptions for contact lenses the Academy states to the Congress that such action by the FTC is not only in excess of its jurisdiction but also endangers the public health.

The FTC announced on May 30, 1980, in the Federal Register, (pages 37051-53) its intention to initiate advance notice of proposed rulemaking procedures (ANPRM) concerning an amendment to the Eyeglasses Rule and Eyeglasses II (16 C.F.R. Part 456). The amendment proposed by FTC staff concerns a "re-release" procedure requiring a seller of spectacle lenses to return the eyeglass prescription or a duplicate to the consumer after the prescription has been filled or refilled, and the release of complete contact lens specifications after the initial fitting so that consumers could comparison shop for additional lenses from other providers.

The Academy has no objection to the concept that the optician who dispenses a pair of eyeglasses from a written prescription of a physician or other licensed provider should return either the original prescription or an exact copy of such a prescription to the patient for the patients records. Should the patient decide in the future to take that prescription and engage in comparison shopping for replacement spectacle lenses, this consumer activity is encouraged by the Academy.

The Academy has a different view with regard to release of contact lens specifications to patients for comparison shopping for replacement contact lenses. The Academy strongly opposes such contact lens specifications being utilized as authorization for unlicensed and unsupervised individuals to duplicate these medical devices for use by patients without the quality of manufacture and the adequacy of their duplication being determined by a professional who is licensed and qualified to make these essential determinations.

If the FTC is contemplating amending its rule to the extent that not only the release of contact lens specifications be mandated by Section 456, but also that state laws be pre-empted in order to grant the right to unlicensed individuals to sell consumers replacement contact lenses based upon these release specifications, without their capability of assuming responsibility for the adequacy of the fit of these contact lenses, such actions will place the consumers in serious jeopardy through possible injury and damage to their eyes, including blindness. The Academy submits that such proposed amendment of the Eyeglasses Rule to include the issuance of complete specifications for fitted contact lenses to be used by consumers to comparison shop for unsupervised replacement of such lenses is not in the best interest of the public.

There is a vast difference between the nature and fitting of spectacle lenses and that of contact lenses. Although improperly duplicated spectacle lenses may cause some discomfort and annoyance to the patient during the period of time they are utilized, improperly duplicated contact lenses can and have caused serious eye damage to the eyes of consumers requiring medical treatment. The many volume chains that have evolved in the past few years to provide duplicate spectacle lenses and contact lenses at reduced "bargain basement" rates uniformly do not assure the high quality of their products or services. They have no professional responsibility to the consumer since they only "duplicate" the prescription specifications and not the fitting. It is the prescriber, viz., the physician or other licensed practitioner, who is responsible for the adequacy of the specifications and the safety of the fitting.

Since improperly duplicated contact lenses, not worn under careful supervision by a licensed physician or other licensed and qualified practitioner, have resulted in serious damage to eyes, it is the position of the Academy that the release of complete contact lens specifications after the initial fitting should be left to the discretion of the physician or other licensed and qualified provider after proper assessment of the consumer's specific and individual requirements. Any contemplation by the Commission to pre-empt state laws to allow any unlicensed individuals to provide unsupervised replacement contact lenses to patients would be a serious threat to the eye health of the nations consumers.

The Academy has recommended strongly to the Commission that it not amend 16 C.F.R. Part 456 requiring release of complete contact lens specifications for the purpose of comparison shopping by consumers. Somewhere in the broad concept of protection of consumers from unfair trade practices there must be recognition of the need to protect the consumer from injuries that can be inflicted by medical devices duplicated improperly, though inexpensively, without adequate professional supervision by those trained, qualified and licensed to provide such services.

A copy of the Comments of the Academy, the American Association of Ophthalmology and the Contact Lens Association of Ophthalmologists to the FTC in Eyeglasses II is attached and it is requested be made part of the record.

While the Academy has supported legislation which would have exempted the learned professions of theology, law and medicine from the antitrust laws as being the more desirable approach to remedy the problem arising from the efforts of the federal government to invade and regulate state licensed professions, it supports S. 1984 as legislation needed to correct abuses of power in state regulated areas by the FTC. This five person Commission is not qualified to override state licensing laws, rules and regulations mandating how the public health is to be cared for in the states, a local reserved state area of operation, in the public interest of the residents of the states.

Senator Melcher in submitting S. 1984 to the Senate for appropriate actions stated it is a step in a "3-year bipartisan effort to reform the role of the Federal Trade Commission regarding its authority over state regulated professions." Senator Melcher further stated during last year's consideration of S. 1991 the similar amendment to that bill sponsored by Senator McClure and himself was lost by a narrow 45-47 vote under the threat of a presidential veto and a sweet promise of oversight hearings. The Senator further stated "Unfortunately, the expanding elasticity of the interstate commerce clause through case law and the insatible demands of federal government regulation have subverted the federal system. Legislation is essential to reverse its direction."

Continuing, the Senator stated that "FTC is one prime tool in the denigration of our state's police powers, it has exceeded its statutory mandate. All states supervise and regulate the delivery of medical and legal care to their citizens. * * * By nullifying these the FTC has sought to make national standards for circumstances which cry out for local and regular variations to fit community needs."

The Senator also opposed FTC activity into the field of professional regulation because first, "the activities of professionals are different from those of * * * merchants" and, second the existing mechanisms for regulating professionals are working well and should be encouraged, and not crippled as the FTC is attempting to do."

The Senator stated he could see no good coming from further agency activity in the area of professional regulation and saw only arbitrary and inept rules that could change the nature of professional practice without any discernable benefit to clients and patients. The Senator being a veterinarian, stated he was quite upset by the FTC's investigation of the veterinarian profession and while this investigation was terminated, nevertheless the FTC still retains under its perception of its jurisdiction authority to re-institute this or other investigations of a similar nature.

Senator McClure of Idaho, in supporting S. 1984, stated he was pleased to report that Senators Goldwater, Heflin, Pressler and Exon had joined in co-sponsoring this legislation making it a bipartisan effort and the House in dealing with similar legislation has well over 100 cosponsors. These cosponsors now exceed 160.

Senator McClure points out that the bill is not limited to clarifying the relationship between the professions and the FTC but deals with the FTC procedures which are inherently unfair for parties before the Commission.

Senator McClure summarized his objections to present FTC procedures as follows: "Accordingly, we address three major areas: The traditional state responsibility for legislative and regulatory action in our Federal system; the ability of professions and their associations to develop meaningful standards of professional conduct to protect the public; and the basic unfairness of the process that subjects groups to FTC fishing expeditions and allows the Commission to be judge, jury and prosecutor on the same case.

* * * * * * *

"I think it is time to restore some equity to the FTC's adjudications."

S. 1984 corrects the procedural inequities of the FTC's enforcement proceedings

Under the present FTC Act as amended, enforcement proceedings are initiated by an FTC complaint before an administrative law judge, an employee of the FTC. Injured respondents then have a limited appeal to the full Commission. From the full Commission's decision on appeal, a respondent has the right to initiate a petition in a Federal Court of Appeals for a review of the Commission's action. This appeal is rather restricted. S. 1984 seeks to correct the inequities involved in this type of an enforcement proceeding by requiring the FTC to file a complaint and try that complaint on the merits in a Federal District Court. The bill further provides for a right of appeal from the District Court's decision to the Federal Court of Appeals where the appeal will be adjudicated as are all other appeals from District Court decisions. The bill further authorizes the FTC, instead of seeking restraining orders from an employee, to seek such a temporary restraining order or a preliminary injunction before a Federal District Court. When such an order is filed if a complaint is not filed within 20 days from the date of the order it is to be dissolved. The bill further provides that the intervenor programs now funded by the FTC are to be abolished and where the FTC seeks to obtain data by subpoenas issued by a District Court the FTC be required to pay reasonable costs and attorneys fees to the person, partnership or corporation complying with any such request.

As the FTC has targeted the American Medical Association, the American Bar Association, the American Dental Association, numerous other professional associations, including the veterinarian association, at the state and local levels, charging such organizations and their members with restraints of trade in violations of the antitrust laws all of which are heard under these present procedures by the Commission which acts as an inquisitor, prosecutor, judge, jury and appellant reviewer, the changes in S. 1984 are designed to correct the basic unfairness of such protracted and expensive proceedings.

The Constitution by its amendments now provides that no person shall be deprived of life, liberty or property without due process of law. Over the years, the Supreme Court has announced the doctrine that proceedings against the people must be fair and must have that appearance of fairness needed to afford the accused due process. The Supreme Court has voided proceedings where the presiding officer in state court proceedings has an interest, though indirect, in the outcome of the proceedings (*Tumey* v. *Ohio,* 273 U.S. 510, 535, 45 S.Ct. 390) and has also voided proceedings where the presiding judge becomes personally involved in the controversial areas involved in federal litigation (*Offutt* v. *United States,* 348 U.S. 11, 14, 75 S.Ct. 11, 16, holds: "Therefore, justice must satisfy the appearance of justice.")

When we compare the present FTC proceedings of a star chamber nature with the more equitable procedures provided for in S. 1984 the Academy submits that basic due process supports the procedures set forth in S. 1984 under the fairness doctrine. As we have pointed out, Senator Melcher stated in supporting S. 1984 that the arbitrary and inept rules being applied under the FTC's present procedures involve practices without any discernable benefits to clients or patients.

The Academy supports the announced views of Senators Melcher and McClure and urges Congress to enact S. 1984 into law in the public interest.

The doctrine of Parker v. Brown bars FTC's intrusion into the regulated learned professions particularly the profession of medicine

The efforts of the FTC to preempt and override state laws regulating the professional practices like the practice of medicine, invade an area that the Supreme Court has announced is exempt from federal antitrust laws which includes the FTC Act as amended. In *Parker* v. *Brown,* 317 U.S. 341 (1943), 635 S.Ct. 307 the Supreme Court forcefully announced that state authorized programs under the reserved police powers of the states are exempt from the antitrust laws of the Federal government. In *Parker,* a producer and packer of raisins, filed a suit against the State Director of Agriculture, Raisin Proration Zone No. 1, because nearly one-half of the world crop of raisins are produced in Raisin Proration Zone No. 1, and ninety to ninety-five percent of such raisins grown in California are shipped in interstate and foreign commerce as an illegal interference and an undue burden upon interstate commerce in violation of the Federal Constitution and the antitrust laws. After a trial, a three judge District Court held the program was an illegal interference with and an undue burden upon interstate commerce in violation of the commerce clause and the Sherman Antitrust Act and enjoined the program.

The Supreme Court reversed, holding the prorate program derived its authority and its efficacy from the legislative command of the state. The Supreme Court found nothing in the Sherman Act or in its history which suggests its purpose was to restrain a state or its officers or agents from activities directed by its legislative (p. 350). Thus the Supreme Court held (p. 352): "The State in adopting and enforcing the prorate program * * * imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit. Olsen v. Smith, 195 U.S. 322 * * *."

While the Supreme Court found as the claim that ninety-five percent of the California crop finds its way into interstate or foreign commerce, and the program adopted by the program committee controls the marketing of the crop so as to enhance the price and maintain prices by restraints on competition of producers (like the plaintiff) in the sale of the crop and eliminated competition of producers, including price, which would have "a substantial effect on interstate commerce", yet the Court concluded (p. 368) "* * * that the California prorate program of the 1940 raisin crop is a regulation of state industry of local concern which, in all circumstances of this case * * * does not impair national control over commerce in a manner or to a degree forbidden by the Constitution." In *Parker* all restraints of the type usually forbidden under the federal antitrust laws were involved. including *per se* actions like controlling the market, enhancing the price, maintaining prices, fixing prices, restraining competition, all of which had a substantial effect on interstate commerce yet the Supreme Court upheld state authority in these areas. It can hardly be said that state licensing laws of physicians in any way resemble the state restrictions and restraints involved in *Parker*, hence the Academy submits that *Parker* bars the FTC from preempting and overriding under its announced plan all state laws, rules and regulations which the five member commission determines "burden" interstate commerce.

We must recognize that the practices of licensed professions, particularly the licensing of the healing art of physicians, are clearly state actions intrastate in character, initiated by the state to cover local conditions and as such are exempt from the antitrust laws as held in *Parker*.

The *Parker* v. *Brown* doctrine clearly supports the enactment of S. 1984 in order to prevent further intrusions by the FTC into laws, rules and regulations relating to the public health enacted by the states covering local problems now well controlled under the reserved police powers of the states.

The Academy thanks the Committee for the opportunity to file this statement in support of S. 1984 and offers its cooperation in the enactment of this needed legislation.

STATEMENT OF THE AMERICAN MEDICAL ASSOCIATION

The American Medical Association submits the following statement in support of S. 1984 for the record and to supplement the testimony presented before the Subcommittee at its July 1981 hearing.

S. 1984 contains amendments to the Federal Trade Commission Act to: (1) makes it clear that the FTC does not have jurisdiction over the state-regulated professions; (2) preclude pre-emption of state laws by the FTC; (3) provide the financial relief from excessive demands of the agency for information; (4) circumscribe the overly broad subpoena power of the FTC; (5) clarfiy the criteria for a finding of "unfair competition;" (6) require the FTC to pursue actions in the Federal Courts to afford defendants the protections of judicial proceedings; and (7) repeal the "intervenor program" so that the agency would not fund individuals and organizations pressing a cause before the FTC. The AMA strongly supports passage of S. 1984.

COMMENTS

S. 1984 contains a number of provisions that are designed to place some limitations on the jurisdiction and actions of the Federal Trade Commission and has the support of both the business and professional community. Since 1914, when the Commission was established by Congress to protect the interests of consumers and curtail the run-away tactics of "big business" that could defraud the public, Americans have become increasingly sophisticated in making purchasing decisions and reliance on advertising puffery. The need for an almost totally independent federal agency to act paternalistically in this field is questionable at best and doubtful in view of the Commission's record.

Both business and the professions have been exposed to the awesome powers of the Federal Trade Commission and can attest to the costly procedures that are entailed in Commission investigations, complaints and rulemaking proceedings. The time has come to weigh the benefits of continuation of FTC power unchecked by judicial safeguards or public scrutiny. It was the Commission's record of legislating and expanding its own authority beyond the intent of Congress that led to a protracted debate in Congress concerning the Commission's role in today's marketplace. The Senate has agreed that oversight is necessary to prevent abuses of unbridled power.

On March 23, the United States Supreme Court failed to resolve the issue of FTC's jurisdiction over not-for-profit professional associations and regulation of the ethical guidelines for the medical profession. The FTC has been intent on establishing its jurisdiction over a voluntary professional association whose members deal with the life and safety of Americans. The FTC did not bother to conduct any investigation of the Association's positions on physician advertising and solicitation or physicians' contractual relationships with group pre-paid plans and it turned a deaf ear to any efforts on the part of the medical profession to make changes as the law evolved.

When professionals are engaged in self-regulatory activities that protect the public and are in the public interest, such as informing patients without deceiving them, the FTC ought to encourage the activity and not condemn it and the profession.

The vote of the Supreme Court is a clear signal that the debate over FTC's jurisdiction should be a matter of Congressional debate and that Congress provides the proper forum for resolution of the issue. The issue is a close one, as demonstrated by four members of the Supreme Court finding on each side of the issue. Similarly, the U.S. Court of Appeals for the Second Circuit had two votes for and one against. The language of the FTC Act is not clear. Legislative history surrounding the Act indicates there was no intent to have the FTC exercise jurisdiction over not-for-profit professional associations whose members are licensed and regulated by states. For example, in the 95th Congress, the FTC requested specific jurisdiction over "not-for-profit" organizations. This proposal was rejected by the Congress. The more recent history of the hearings in the Senate also indicate how close the question of FTC jurisdiction over not-for-profit professional associations is.

The AMA and other professional associations would like to see this issue resolved in a manner that makes it clear that the FTC does not have jurisdiction to regulate professional associations whose members are regulated by the states. Professional associations are not afraid of being subject to antitrust laws and believe that it is appropriate. The issue of how the antitrust laws are enforced is a different matter, however. Clearly, the courts provide a better forum for resolution of antitrust issues than an independent federal Commission with hearings before an Administrative Law Judge who is an employee of the Commission.

PROFESSIONAL SELF-REGULATION

The learned professions and their professional associations serve the public through responsible self-regulation. The role of professional self-regulation has long been recognized as beneficial to the public interests and is afforded special treatment under the law. The history of self-regulation by professionals has been shown to utilize the expertise of the members of the professions in upgrading educational standards, assuring competent practitioners and protection of the public through peer review activities. The state regulatory agencies for the professions rely in large part upon the self-regulation provided by the members of the professions.

Government does not have the personnel nor the knowledge to regulate the professions in the public interest. By recognizing the importance of professional self-regulation, there is no intent to remove the professions and their associations from enforcement of the antitrust laws. Only the forum would be changed. The U.S. Department of Justice can enforce the federal antitrust laws, state attorneys general have enforcement powers, and civil antitrust actions are available. Enforcement through use of the judicial system better protects the interests of the government, the professions and the public.

PRE-EMPTION OF STATE LAWS

One area of over-extension by the FTC is its continued efforts to delcare the laws of the states to be null and void. We believe that it is totally inappropriate for a nonelected five-member commission to overturn the action of the sovereign states. Such assumption of power undermines our system of federalism.

State legislatures have a better understanding of local conditions and values or may legitimately have a conception of "unfairness" very different from that of five Commissioners in Washington. A Commission whose members are not elected should not be able to pre-empt policy established by elected members of state legislatures.

The proper role for federal and state governments in our system of federalism is a topic frequently dicussed today. Adoption of a limitation of the FTC's ability to preempt state law, as contained in S. 1984, would be a step towards reaching the appropriate balance.

INFORMATION GATHERING AND SUBPEONAS

The FTC's almost unlimited power to collect information allows the agency to go on "fishing expeditions" without probable cause. The FTC has the authority to compel persons to provide information. The cost of providing the volumes of information the FTC demands can be extremely expensive. This cost is borne exclusively by the provider of the information, not the FTC. S. 1984 would reform this FTC activity in two ways. The FTC would have to pay the reasonable cost of complying with an information request, and the FTC would need a court issued subpeona before one could be forced to provide information. Thus an impartial judge would determine if sufficient cause exists to justify requiring production of information. These two measures would provide some protection from costly information requests and still allow the FTC to obtain information needed to do its job.

UNFAIR COMPETITION

S. 1984 would require a showing that there was consumer injury that outweighed any benefits derived from the challenged activity before the FTC could find that the activity constituted an unfair method of competition or an unfair or deceptive act or practice. We believe the FTC recently had far exceeded its authority to regulate false and deceptive act or practice. We believe the FTC recently has far exceeded its authority to regulate false and deceptive advertising and unfair methods of competition.

INTERVENOR PROGRAM

The intervenor funding program allows the FTC to pay attorney fees, expert witness fees and other costs of persons and organizations who represent an interest in a rule-making proceeding. This distorts proceedings before the Commission because participants on one side of an issue are subsidized by the FTC while those with alternative views are forced to devote their own resources. Financial considerations can certainly affect the case presented. As another way of making FTC proceedings more fair, S. 1984 repeals the intervenor program.

ADMINISTRATIVE HEARINGS

Of major concern to the AMA is the basic unfairness one finds when involved in an FTC action, where the Commission acts as inquisitor, prosecutor, judge and jury. S. 1984 provides for such actions to be tried in court before an independent and impartial federal judge rather than in an administrative proceeding before a hearing examiner employed by the prosecuting agency. Appeals would be taken directly to the United States Court of Appeals rather than to the very agency which issued the complaint in the first instance. This change in the law would provide a much fairer method of adjudicating unfair or false and deceptive acts or practices.

CONCLUSION

The AMA believes that the public is better served through professional self-regulation than regulation by FTC. The Association believes S. 1984 would improve the effectiveness of the FTC in regulation of business practices and enhanced consumer protection activities relating to business and industrial practices. The AMA supports the bill and urges this committee to act favorably on it.

STATEMENT OF THE ASSOCIATION OF GENERAL MERCHANDISE CHAINS, INC.

The Association of General Merchandise Chains, Inc. (AGMC) represents 125 retail companies operating more than 20,000 discount, variety, dollar and family center stores. Its members range in size and include not only many of the nation's largest retail chains, but also companies active in one or more regions of the country or in a few localities. AGMC member company stores are found in every state of the nation and last year accounted for over $35 billion in sales.

AGMC wishes to express its profound concern over statements made by some policymakers at the Federal Trade Commission that they disagree with, and would seek to change, a long-established principle of antitrust law: the per se rule of illegality govering resale price maintenance.

On numerous occasions, FTC Chairman Miller has challenged this important safeguard to price competition and stated the view that suppliers ought to be empowered to control the retail price of their goods. This position is clearly contrary to over seventy years of Supreme Court decisions. In our view, it also is contrary to the Congressional interest expressed in the 1975 enactment of the Consumer Goods Pricing Act, which removed antitrust immunity for state "fair trade" laws which similarly allowed suppliers to control resale prices.

Resale price maintenance, as amply demonstrated by experience under state "fair trade" laws, harms consumers, the economy and the efficiency of the nation's system of distribution. Numerous government and private economic studies presented to the Commerce Committee in connection with repeal of anti-competitive state "fair trade" laws documented the billions of dollars in additional costs to consumers directly attributable to resale price maintenance. Hampering price competition will reduce the availability of products, hurt small and large businesses alike and gravely damage the retailing industry, now widely recongized as the most freely competitive segment of the economy. Higher consumer prices caused by supplier-imposed price-fixing will also fuel inflation and hinder the nation's economic recovery efforts.

A retail company's ability to determine merchandise prices free from outside coercion and in light of marketing strategy, consumer demand and preferences and its competitive situation lies at the heart of our industry. Any retreat from the well-established per se ban on resale price maintenance will remove this crucial safeguard to a competitive retail marketplace.

Until directed otherwise by Congress, the Federal Trade Commission should continue to enforce this well-established rule of law banning resale price maintenance, rather than attempt to overturn it. AGMC urges the subcommittee and full Committee to see that the Congressional intent expressed in repeal of "fair trade" is carried out in Federal Trade Commission policy towards resale price maintenance.

STATEMENT OF GERALD J. THAIN

INTRODUCTION

Since 1974, I have been a Professor of Law at the University of Wisconsin, and during that period I have served as co-director for clinical education of the Center for Public Representation—a non-profit public interest law firm in Madison, Wisconsin. Prior to 1974, I served at the Federal Trade Commisson—first, in the Office of General Counsel (Division of Appeals), 1963–69, subsequently as attorney-adviser to Commissioner Philip Elman, 1969–70, then as director of National Advertising Regulation division, 1970–73, and finally as assistant to the Director, Bureau of Consumer Protection, 1973–74.

My statement is in response to certain proposed amendments to the Federal Trade Commission Act concerning the jurisdiction of the FTC over the trade activities of professionals, and the definitions of unfair and deceptive acts or practices. For the reasons that follow, I am of the firm opinion that the proposed changes are not only unnecessary but could inflict severe damage on consumers.

A. The regulation of professionals

The Center for Public Representation has been involved in issues of state regulation of the trade activities of professionals and other licensed occupations since 1975. It is quite clear to those who have worked to remove anticompetitive conduct from this arena that, in the absence of federal involvement, the professions would be left largely unregulated. The simple fact of life is that most individual states lack either the power or the will for effective oversight and control of the trade activities of the licensed occupations. For example, strenuous efforts by the Center, supported by the then Dean of the Law School, to lift some of the restraints existing in the mid-1970s on lawyer advertising so that potential consumers of legal services could be provided more information, were totally rebuffed by the anti-competitive stance of the bar leadership until the Supreme Court decision in *Bates & O'steen*[1] forced the addressing of this issue.

The problem is not singular to Wisconsin. In *Goldfarb* v. *Virginia State Bar*,[2] the state bar of Virginia had gone so far as to engage in the most obvious type of anti-consumer conduct—price fixing achieved by the establishment of minimum fee schedules. In the *Bates* decision, the State of Arizona had authorized the state bar to prohibit lawyers from any type of advertising, frustrating the ability of consumers to receive the most elementary information. Provision of the basic information that "X drug is sold by us at Y price" was denied consumers by the State of Virginia prior to the Supreme Court decision in the *Virginia Pharmacy*[3] case. Many more examples could be cited. See generally *Occupational Licensing*[4] by Benjamin Shimberg. This illustrates the historic inability of individual states to free themselves effectively from the control of professional groups in order to regulate the trade conduct of such groups in the public rather than the professionals' interest. It should be emphasized that the FTC jurisdiction in question relates to concerns about the trade conduct of such groups as lawyers, physicians, dentists, accountants, etc. The theory that the professional or licensed occupation status of these groups should provide them with immunity from the fundamental rules governing competition—such as prohibition of price-fixing and bans on providing information about their services to consumers via advertising is devoid of merit. (One suspects that this theory plays a large role in the efforts of so many occupational groups to achieve "Professional" status.) Mere possession of a graduate degree should not be tantamount to a license to engage in anti-competitive and anti-consumer conduct.

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[1] *Bates* v. *State Bar of Arizona*, 433 U.S. 350 (1977).

[2] 421 U.S. 773 (1975).

[3] *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council*, 425 U.S. 748 (1976).

I am thus wholly in agreement with Chairman Miller and the other member of the Commission that the consumer's interest is best served by maintaining the jurisdiction of the FTC over the trade practices of professionals such as lawyers and physicians. It is not the consumers of these professional services who find federal jurisdiction inappropriate—it is the "trade unions" of the professions who object to being held to the same standards as others.

B. The redefinition and codification of "Unfair . . . acts or practices"

Changes proposed in the standards by which advertising practices are classified as "unfair," seem to stem essentially from a concern that the current standards are intolerably elastic. It should be noted, however, that the criteria articulated by the Supreme Court in the *S&H*[5] case by which a practice may be judged unfair, are no more amorphous or less workable than those commonly employed in this country's law. It is the norm for an administrative agency to be delegated the power to license or regulate in the "public interest, convenience and necessity"—the ICC and the FCC are just two of many federal agencies with such mandates and many state agencies have been delegated similar mandates. Forty-nine states have adopted the Uniform Commercial Code, Section § 2-302 of which prohibits "unconscionable" transactions. (The distinguished group of practitioners and scholars writing the Code found it necessary to prohibit a mode of conduct, and vital to avoid enactment of a laundry list of explicit forbidden acts—a good indication of the soundness of the use of such language as "unfair practices" of "public interest," in legislation delegating administrative authority.) "Unconscionability" and "Public interest, convenience and necessity" acquire definition as technology as well as policy and case law evolve; the standards are necessary flexible to meet changing circumstances. No convincing reason has been presented to show that the "unfairness" standard need develop any differently.

Every state now has a "Little FTC Act" which provides for the Attorney General's office, or a like body, to take action against unfair or deceptive advertising practices within the state. Many states, like Wisconsin,[6] adopt FTC decisions as precedent for purposes of administering the state act. Other states routinely amend their acts to conform with changes in the FTC Act. To the extent that the states model their acts and law after the FTC, restricting the FTC's power to attack unfair advertising practices may similarly restrict the power of the states, and provide incentives for unscrupulous actors to test the limits of state authority over "unfairness."

As to the proposal that the FTC's December 17, 1980 policy statement defining unfair acts or practices be codified, there is little to be gained and much to be lost by such action. A general statement of agency policy provides applaudable clarification for businesses enabling them to predict what will and will not be attacked as unfair. Enacting such a standard into law is an entirely separate matter. Absent some showing that the FTC has routinely ignored its 1980 policy statement (which has not, to my knowledge, even been suggested) no significant benefit would be obtained by adoption of the present policy statement, and such codification would freeze if not atrophy the unfairness standard. In an age described by author Alvin Toffler as one of "future shock" where we as a people are barely able to cope with the frantic pace of social and technological change, it makes little sense to cement the definition of an unfair act or practice in a given time and place, when the progress of technological developments is hyper-dynamic rather than static.

Even today, the proposed amendment would apparently exclude from FTC review certain practices which I think most dispassionate observers would agree to be appropriate subject matter for FTC regulation. The three suggested criteria which must be established before a practice may be attacked as unfair, are 1) that the harm to consumers be significant; 2) that the harm outweigh any benefits that may accrue from the practice, and 3) that consumers could not reasonably have avoided the harm. Vulnerable purchasers generally stand to lose a great deal by adoption of the revised definition of unfair practices. Examples include victims of high pressure sales tactics and purchasers of funeral services.

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[4] B. Shimberg, *Occupational Licensing: Practices and Policies* (1973).
[5] *FTC* v. *Sperry & Hutchinson,* 405 U.S. 233, 244-5 n. 5 (1972).
[6] See Wis. Stat, §§ 100.18, 100.20 (1979).

i. High pressure sales

No deception, in the traditional use of the word is necessarily involved in the intensive door to door selling of brushes, encyclopedias, vacuum cleaners or what have you. At the same time, the harm involved in the systematic and repeated harassment of potential buyers, ultimately resulting in sales that would not otherwise have occurred, is impossible to quantify and coherently balance against any benefits flowing to consumers as a result of the sale. A "reasonably" consumer is always able, in theory, to say no to a door to door salesman; the fact that repeated harassment may neutralize the purchaser's capacity to make reasoned decisions would make no difference in the sense that the quintessentially reasonable person should still be able to decline the seller's offer, and thus the practice could not be classified as unfair. Economists and social psychologists alike generally agree that the predilection of individuals to act in their own economic interest is varied immensely by their personal preferences which determine their responses to given situations. One for whom courtesy and etiquette are paramount values is unlikely to act in an "economically rational" fashion and slam the door in a seller's face. And marketeers know and attempt to take advantage of this. Why should the law ignore it?

ii. Purchasers of funeral services and other vulnerable consumers

The casual purchaser of funeral services has suffered recent and significant loss of a friend or loved one. In such a state, the buyer is particularly vulnerable and may be taken advantage of in a way that would not occur under normal circumstances. Yet the proposed redefinition of unfairness requires that the practice be evaluated in terms of whether an objectively reasonable person could have avoided the unfair treatment—no allowance is made for the subjective state of vulnerable purchasers.

The proposal does extend protection to especially vulnerable audiences, if it can be shown that the advertiser intended to mislead or take advantage of the viewer or listener. But the FTC mandate has been to prevent unfair or deceptive practices and their effects from occurring in the future, not to punish the guilty mind for improper deeds committed in the past. If a particular trade practice in fact misleads or takes advantage of consumers, that may well be a valid consideration in beginning the pursuit of the matter; however, it is no justification for conditioning the FTC's statutory authority to order amends for the practice upon the advertiser's state of mind.

iii. Judicial review

Even more significant in the proposed changes in the definition of unfair acts or practices would be the impact of the proposal upon judicial review. As it stands, the Administrative Procedure Act essentially requires that courts affirm the decisions of FTC adjudication when such decisions are supported by substantial evidence. Thus, courts may evaluate an FTC adjudication of an unfair practice in terms of whether the FTC's determination that the practice is "unfair" within the meaning of the statute was supported by substantial evidence. By contrast, if the Federal Trade Commission Act were amended to include the proposed definition of unfairness, considerably elongated review proceedings may well result. Reviewing courts presumably would be required to apply the substantial evidence standard to each of the three components of the proposed definition of unfairness, inquiring into the sufficiency of the evidence that the consumer injury was "significant," that the injury outweighed benefits to consumers and that the consumers could not reasonably have avoided injury. Given the recurrent problem of backlog in the courts, a new law requiring extended and more detailed inquiry in review proceedings (and greater possibilities for remand rather than direct decision-making) would *not* promote judicial efficiency.

C. Deceptive acts or practices

Chairman Miller, unsupported by other Commissioners, has proposed that a definition of deceptive act or practice be incorporated into the FTCA, providing 1) that the challenged act or practice injures consumers; 2) that the challenged act or practice involve statements or representations of fact, not opinion; and 3) that deception be measured by whether reasonable consumers are likely to be deceived, with protection of vulnerable groups effected by concentrating on whether the advertiser intended to deceive or mislead.

From the outset, it is unusual at the very best that Chairman Miller would propose statutory changes in the definition of deception that were not earlier suggested by the remainder of the Commission, or by consumer groups, or by the AAF, or by the American Association of Advertising Agencies, or by the ANA. Affected interests are accustomed to the current definition that has been fleshed out by over 40 years of case law. Change for its own sake, which is what Chairman Miller proposes, is of dubious merit.

Limiting the scope of deception to practices that mislead only a so-called reasonable consumer would have several adverse consequences. First, to presume that consumers can and do consistently make "reasonable" decisions as a matter of course is simply myopic. In the case of fungible consumer goods, e.g., lemon juice or bleach, a rational consuming public presumably would have no reason to favor one brand over another. Yet, one manufacturer in both of these areas has been able to dominate the market and at the same time maintain a price per item that is considerably higher than that of competitors. One must conclude either that "reasonable consumer" is a contradiction in terms, or, more accurately, that generally "reasonable" consumers sometimes make "unreasonable" decisions. If "reasonabless" were the biggest factor in the marketplace, the demand for market research explaining consumer motivation and for efforts by sellers to respond to such motivations would be largely eliminated. A world of consumers engaged in only "reasonable" decision-making would strike many as uniform and dull—perhaps a reason why traditional economics is sometimes dubbed "the dismal science."

Moreover, what is reasonable for a given consumer under one set of circumstances may be clearly unreasonable under another. The idea that "reasonable" is a word providing stability to the law is simply an illusion.

Implementation of a "reasonable consumer" standard would add another variable—and greater uncertainty—to the determination of whether a particular practice was deceptive. Indeed, an expecially cynical person might suggest that this was the motivation behind the proposal. As the law now stands, the Commission need only establish a tendency or capacity to deceive a not insignificant percentage of the public; the practice must be evaluated to determine if it is likely to mislead viewers or listeners, sophisticated and credulous alike. Under the proposed amendment, however, not only the practice, but the viewers and listeners as well must be evaluated to decide whether those who were or could have been deceived, were also "reasonable" as Chairman Miller would define that word. Is the average viewer of advertisements run during a televised opera or theatrical production to be held to the same standard of "reasonableness" as one watching Saturday morning cartoons? How is the reasonable consumer to be defined, given the fact that decision making based on extra-rational factors is a commonplace? These questions do not present obvious answers, and make increased reliance upon psychological evaluation, testimony, and their concomitant expense inevitable.

Chairman Miller, who is not a lawyer, insists that " 'reasonable' . . . has a special and well understood meaning to lawyers." This may be an accurate statement, in the context of common law negligence, where there is something close to consensus as to how a reasonably prudent individual is expected to respond in a given situation which places him in potential danger. By contrast, there is no shared understanding of what constitutes a reasonable response to advertising or other selling practices. Some economists may define reasonableness in terms of whether the consumer based the decision to purchase upon considerations affecting price and quality. Some psychologists, and certainly many advertisers, on the other hand, expect a "reasonable" consumer response to include consideration of extra-rational factors. Indeed, why would advertising go to the trouble and expense of making claims that a product adds life, enhances sex appeal, makes a man smell like a man, and so forth, if consumers did not in fact respond to such claims? To assess the deceptiveness of an advertisement solely in terms of its impact upon "Chairman Miller's reasonable consumer" is to ignore the increasingly visible and vast body of research in the field of consumer psychology attesting to the fact that consumer behavior is not controlled by factors regarded as "reasonable," as the term is traditionally defined.

The Chairman's proposed standards under which the FTC could attack an act or practice as deceptive, are essentially the same as those defining the common law tort of misrepresentation. The tort of misrepresentation, like the proposed definition of deception, requires that the purchaser be reasonable misled by the seller's representation, resulting in measurable injury to the purchaser. The phenomenally complex and often subtle nature of deception in advertising and selling renders it unsuitable to treatment under these misrepresentation standards. For the reasons outlined above, it is unhelpful to assess the reasonableness of consumer responses to advertisements when extra-rational factors influence, and sometimes control, decisions of otherwise reasonable consumers. It is similarly inappropriate to condition a deceptive advertising action upon a finding of measurable consumer injury directly related to a misrepresentation; often, a consumer purchases a product for many reasons, Chairman Miller's proposal would ignore blatant misrepresentation inducing purchases so long as there were other intertwined reasons for the purchase. The result would be an invitation to sellers to ignore truthfulness in preparing their pitches.

It is one thing to establish, as the Commission already has, that, as a matter of policy, it is appropriate to take action only against those advertising practices which result in substantial injury to consumers. It is another thing altogether to statutorily bind the commission to such a policy, for to do so would be to deny the Commission the authority to act in situations where exceptions to the policy would be appropriate.

Timothy Muris of Chairman Miller's staff, characterizes the nature of actionable consumer injury as follows:

"To determine if consumer injury is likely, the key question is whether consumers have given up something of value if the claim is false . . . [I]t is unlikely that consumers will give up anything of value unless the product is worth more if the claim is true than it is worth if the claim is false."

How can one assign "worth" to the psychic injury associated with a false claim that a product is kosher or vegetarian when it is not? Moreover, were the FTC prohibited by law from taking action against advertisers in all cases where the product in question would be worth no more were the false claim true, the integrity of the entire marketing process would be threatened. By permitting as a matter of law, seemingly innocuous false and deceptive claims, public perceptions of accuracy in advertising would be irreparably damaged. It would take no more than a smal handful of unscrupulous advertisers, unconcerned about the accuracy of their representations in the absence of any threat of public legal sanctions, to destroy public perceptions of legitimacy in advertising and advertising regulation as a whole. A "free-fire zone" for deceptive advertising would be the inevitable result of adopting Chairman Miller's proposal.

In conclusion, what Chairman Miller's proposal fails to recognize is that the law on paper does not always emerge as the law in practice. The hypthetically reasonable consumer is reduced to a useless fiction in a context in which purchasing decisions are swayed by a multimillion dollar industry expert in sophisticated techniques of consumer seduction. A required showing of measurable consumer injury likewise fails to adequately protect the consumer interest in practice. I therefore urge that the proposed amendment to the FTC's authority over deceptive acts or practices be rejected.

CONCLUSION

The costs of removing FTC jurisdiction over the licensed occupations and redefining "unfairness" and "deception" insofar as the FTC's authority over such practices is concerned would be immense consumer injury. The alleged "benefits" of taking such actions are entirely theoretical and have not been demonstrated to bear any relations to the real world of marketing and promotion. The proposed changes should be rejected.

STATEMENT OF EARLE D. BIGGERSTAFF, PRESIDENT, THE NATIONAL FUNERAL DIRECTORS ASSOCIATION

My name is Earle D. Biggerstaff of Caney, Kansas, the owner and operator of two funeral homes. I am the current President of the National Funeral Directors Association.

The National Funeral Directors Association is a federation of state associations. It has 13,478 members. Its members conduct about 65% of the funerals held annually in the United States.

We are filing this statement because your subcommittee is considering the authorization for the Federal Trade Commission for the period beginning on October 1, 1982. We in funeral service are most interested having been the target of FTC activity since November, 1972. It was then that an official of NFDA learned by accident that the FTC was looking at funeral practices and our association. However, it was not until mid-1973 that there was a resolution of the Commission for a non-public investigation which proved to be very public.

During meetings held with members of the funeral rule staff, NFDA and other associations asked for an opportunity to determine whether guides would solve any existing problems—guides in lieu of a rule. NFDA joined with the National Selected Morticians in a formal request for guides. This action resulted in a hearing on March 12, 1976 and just before the fifty-two days of hearings in six cities began in April of that year. The Commission rejected the idea of guides. After many meetings with members of the FTC staff, guides were again requested and rejected (December, 1980).

Coincidental with the initial study of funeral service by the FTC (1972) an approach had been made by NFDA to the Office of Consumer Affairs for a consumer program. Nothing developed. In 1980 another approach was made and Mrs. Esther Peterson was invited to speak at a meeting of NFDA's state association officers in Reston. She could not accept because of a previous commitment but sent her counsel.

In mid-1981 during a meeting with Virginia Knauer and some members of her staff, ThanaCAP was conceived as a consumer action panel part of a funeral service consumer program. It was born later by an overwhelming vote of the NFDA House of Delegates meeting at the association's Centennial Convention in Boston, October 25-29, 1981. Virginia Knauer and members of her Consumer Affairs staff have been most cooperative and helpful.

The proposed funeral rule submitted to the Office of Management and Budget on March 17, 1982 is opposed by NFDA. The opposition is based on 1972, 1976, 1979 mandates of our House of Delegates which in 1981 also voted to support a Congressional veto of a rule.

Here follows a brief synopsis of NFDA's opposition to the funeral rule and support of a Congressional veto:

(1) The record relating to a proposed rule for funeral industry practices taken as a whole does not indicate the prevalence of unfair or deceptive acts or practices by funeral directors.

(2) If the rule as submitted to the Office of Management and Budget becomes a reality it will work an unfair and unwarranted disadvantage on funeral directors. The rule would cover only those who provide both funeral goods and services. Funeral directors compete with those who provide only goods and also those who provide only services. Such competition is increasing. In the short time ThanaCAP has been publicized, there have been more inquiries and complaints about those in funeral service not covered by the proposed rule than there have been as to funeral directors and their practices which only would be covered by the rule.

(3) "The number of consumer complaints filed against funeral directors is indeed modest and consumers are generally satisfied with the performance of funeral directors." This is the statement of a former FTC staff member which is in the record.

(4) In the rule the FTC is mandating the availability of certain merchandise and specific services or forms of disposition. Freedom of choice of the funeral director to provide services deemed proper is abridged. No other small business that is not a utility is so regulated.

(5) The rule would be a layer of unnecessary federal regulation on top of that of state and sometimes city regulation of the funeral directing aspect of funeral service with no less than 46 states requiring price disclosure.

Over a period of years funeral service and funeral directors have suffered as the result of publicity coming from the Federal Trade Commission. During that time over fifteen million funerals have been conducted with very few complaints even though they have been openly sought by the FTC and some consumer groups.

During the same period funeral service organizations have proposed voluntary programs to try to resolve whatever problems existed. This was done on the basis that if the voluntary programs didn't work, then a mandatory rule would be justified. These proposals were rejected. Had the proposal made by funeral director associations in 1976 been put into effect for a period of two years, by 1979 there would have been a track record to indicate the need or lack of a need for a rule.

In summary, on behalf of our National Association and our members across the nation, we are asking you and your subcommittee to include in the new authorization bill for the Federal Trade Commission the following: (1) the provisions of a Congressional veto for all FTC trade regulation rules; (2) include therein a prohibition of the finalization of the proposed FTC funeral service rule for the period of the authorization bill; (3) or, include a moratorium on a funeral rule for two years to see what effect ThanaCAP with a majority of consumer panelists will have along with other consumer oriented programs, laws, regulations and guides initiated by the providers of funeral services and others.

STATEMENT OF EDWARD H. MEYER

My name is Edward H. Meyer, and I am Chairman of the Board and President of Grey Advertising Inc. As the Chief Executive of one of the nation's ten largest advertising agencies I work with many of America's leading consumer-oriented manufacturers and service corporations, to whom advertising is virtually the breath of life. I believe the right to advertise openly, freely and honestly and product which it is legal to sell is one of the fundamental principles upon which our free enterprise system is based.

I am, therefore, in favor of legislation like the Federal Trade Commission Act which prohibits false or misleading advertising, because consumer deception injures not only consumers but also honest competitors, and corrupts the operation of the free enterprise system. However, the notion advanced by some that the Federal Trade Commission should have the power to regulate the form and content of truthful, non-deceptive advertising solely to promote its ideas of "fairness" is alien to the free enterprise system. Consequently, I want to urge the Subcommittee to enlarge and make permanent the prohibition of the FTC's efforts to regulate advertising on the grounds of unfairness that was enacted in 1980.

That temporary prohibition applied only to industry-wide rulemaking. It should now be made permanent and incorporated as well into Section 5 of the Federal Trade Commission Act so that it will apply to case-by-case adjudication as well as to rulemaking.

Some say the Federal Trade Commission should promote the efficient functioning of free markets and, to do it, needs authority to dictate the informational content of advertising copy in order to correct market imperfections and ensure that consumers have all the information needed to make rational purchasing decisions. They would do this in the name of fairness, judging as unfair any advertising that failed to meet its informational standards. This kind of censorship threatens the right of free expression, which is fundamental in America, and betrays an ignorance of the role of advertising in our free enterprise system.

Advertising can be defined as a surrogate "salesman," using paid space and time in mass media to reach his customers. That's a vital function in a competitive economy, since it represents the most efficient means to provide consumers with an important source of information on product availability, new products, product improvements, prices, relative performance and product use. In addition, of course, advertising revenue is the foundation of America's free press—the news, information and entertainment in print, radio and television.

The public, as countless studies have documented, is extremely well aware that advertising is not "journalism"—it is not a consumer report but an overt attempt on the part of the marketer to sell his wares. Small children growing up in this country quickly learn to distinguish between commercials and programming, editorial and advertising matter. And no normal adult fails to recognize that advertising's purpose is to persuade him to trade hard-earned cash for a product or service.

I believe that Congressional concurrence in the authority the Federal Trade Commission now claims it has under existing law to regulate advertising copy on the basis of its so-called "fairness" would set a drastic precedent, releasing a governmental force that could dictate a change in advertising's economic role. It would impair not only the advertiser's ability to sell but also the consumer's right to receive information and make his own purchase decisions. Where will the FTC draw the line on its "informational" requirements? Perhaps we will begin to see copy like this:

"Fly *happy* with Smith Airlines—only eight fatalities in the last ten million passenger miles flown."

"See the 1982 Jonesmobile—and we had only sixteen defect notices in 1981."

"Beautiful Colonial, three acres, four bedrooms, good schools—termites, high fuel bills."

I trust my point is clear. The primary economic responsibility of advertising is to sell. That role is extraordinarily well understood by the American public.

In summary, I sincerely believe that the failure of Congress to deny the FTC the power to regulate the content of non-deceptive advertising would strike at our First Amendment right of free speech and the consumer's right to be freely informed about products and services without undue restriction or bias, which is fundamental to our free enterprise system. Sellers must be free to advertise their lawful products in a truthful, non-misleading manner.

Government regulation of advertising content in the name of high-sounding public and social policy goals, however well intentioned, could very well lead to measures by the "fairness" enforcers to mold citizens' beliefs, attitiudes and actions rather than to ensure that the public is honestly alerted and aware.

STATEMENT OF BRUCE A. SILVERGLADE, DIRECTOR OF LEGAL AFFAIRS, CENTER FOR SCIENCE IN THE PUBLIC INTEREST

The Center for Science in the Public Interest (CSPI) appreciates this opportunity to submit its views on the reauthorization of the Federal Trade Commission (FTC).

CSPI is a non-profit consumer information and advocacy organization and has a longstanding interest in improving national health policies. We are supported by the donations of our 35,000 individual members, sales of publications, and foundation grants. We accept no funding from either government or industry.

For the last ten years, we have been particularly concerned about the effects of national advertising on the health and well-being of consumers. On numerous occasions, we have filed complaints with the FTC and have relied on that agency to take action against unfair and deceptive advertising. For example, we have requested the FTC to act against advertising that misleadingly portrays the nutritional benefits of white bread,[1] tha misleads consumers about the safety and efficacy of over-the-counter drugs,[2] and that exploits the vulnerabilities of children by encouraging them to consume highly sugared cereals, candies and other products that may harm their health.[3]

We are therefore extremely concerned about proposals to prohibit the Commission from acting against "unfair" advertising.[4] In particular, we believe that such proposals endanger the public health because they would render the Commission powerless to act against advertising that threatens the health and safety of consumers.

The prohibition on FTC scrutiny of unfair advertising is primarily supported by the American Advertising Federation, Association of National Advertisers, and the American Association of Advertising Agencies. This proposed exemption seriously threatens consumers' health and well-being, and is, furthermore, unjustified and discriminatory.[5]

The proposal specifically calls for the FTC to be permanently prohibited from acting against unfair advertising on a case-by-case basis.[6] If this proposal is enacted, the FTC will not be able to act against many advertisements that not only cause economic harm, but also endanger the public health. In the past, the FTC has utilized its authority to restrict particular cases of such advertising on the basis that they were "unfair."

For example, the FTC prohibited an advertiser of razor blades from promoting its product by inserting a free sample blade in the comic section of metropolitan Sunday newspapers. The Commission found that it was an "unfair" advertising practice to insert a razor blade in the Sunday comics, where young children might find the blades and be injured.[7]

In other cases, the FTC prohibited advertisers from depicting dangerous conduct, such as a young child cooking food on a stove or using an electrical appliance near water. These advertisements were viewed by children who might imitate the unsafe behavior and were prohibited in accordance with the Commission's authority to restrict unfair advertising.[8]

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[1] *In Re ITT Continental Baking Co.*, Complaint to prohibit false and deceptive advertising, July 24, 1981.

[2] *In Re SmithKline, N.W. Ayer*, Complaint to prohibit unfair and deceptive advertising, October 19, 1981.

[3] In the Matter of Children's Advertising, 43 Fed. Reg. 17987 1978.

[4] Presently, Section 5 of the Federal Trade Commission prohibits "unfair or deceptive acts or practices in or affecting commerce," 15 U.S.C. §45(a)(1).

[5] We note that the advertising community has also proposed changing the definition of deception, as recommended by FTC Chairman James C. Miller III. This proposal has been comprehensively analyzed by Consumer's Union in testimony and other supplementary materials submitted to this subcommittee. We concur with CU's analysis of this proposal. We also note that this proposal, if enacted, would seriously endanger the public health because it would hinder the FTC from acting against misleading advertising for food, drugs, alcoholic beverages and other products that affect consumers' health and well-being. Our remarks here, however, are confined to the proposed exemption for advertisers from FTC unfairness authority.

[6] This proposal also calls for a permanent extension of the present ban on FTC authority to issue trade regulation rules that would restrict "unfair" advertising, 15 U.S.C. §57a, note.

[7] *Philip Morris*, Inc., 82 FTC 16 (1973).

[8] *Uncle Bens, Inc.*, 89 FTC 131 (1977); *Mego Intl.*, 92 FTC 186 (1978); see also *AMF, Inc.* C-3011 (1980).

The FTC also relies on its unfairness authority to require the disclosure of health warnings in advertising for various products. For example, since 1972 cigarette companies must include the Surgeon General's warning in their advertising.[9] The FTC also found it was "unfair" not to warn consumers of over-the-counter diet pills that they should not use the drug if they suffered from hypertension or certain other illnesses.[10]

In addition, the FTC has relied on its unfairness authority to substantiate safety claims for products such as swimming flotation devices.[11] It aslo relies on such authority to require advertisers of over-the-counter drugs to substantiate efficacy claims.[12] In addition, the FTC's unfairness authority prevents advertisers from directing claims to particularly vulnerable individuals who are incapable of making a rational purchasing decision. For example, ads that claimed women could alleviate marital problems by taking the stimulant Vivarian before their husband arrived home in the evening have been prohibited.[13]

In taking action against such practices, the FTC has relied on its unfairness authority because such advertisements are not necessarily deceptive. If advertisers are totally exempted from FTC's jurisidiction over "unfair" business practices, the FTC will not be able to effectively restrict such advertising in the future.

Furthermore, a special exemption for advertisers from FTC unfairness jurisdiction is unjustified and discriminatory. There is no reason why advertisers should be granted special privileges to engage in unfair business practices. Advertisers, claim they deserve an exemption because FTC has abused its authority in the past. While we disagree with these contentions, we note that Congress, the Supreme Court and the FTC itself have all taken steps in the last two years that would protect advertisers from any purported abuses in this area.

First, in enacting the FTC Improvements Act of 1980, Congress prohibited the Commission from issuing any trade regulation rules based on its "unfairness" authority. While we do not agree with this prohibition, we note that it ensures that the FTC can only use its authority narrowly, on a case-by-case basis.

Second, the Supreme Court, in *Central Hudson Gas and Electric Corp.* v. *Public Service Commission of New York,* 447 U.S. 557 (1980), has defined the limits of constitutionally protected speech. In this case the Supreme Court announced a four-part test that prevents the FTC from abusing the use of its authority to restrict "unfair" advertising. This test first requires agencies such as the FTC to determine whether an advertising claim is true or false. If the advertising is technically true, but still objectionable, the Commission cannot act unless it determines:

A substantial government interest would be served by restricting advertising;

The restriction would "directly advance" the public interest;

The restriction would not be overly broad and lesser remedies would not be sufficient.

Third, the FTC itself has adopted a formal statement of policy explaining how it intends to further limit the use of its authority to restrict "unfair" business practices. Before the FTC acts against any "unfair" practices, it must demonstrate that:

The practice causes substantial economic injury to consumers,

Consumers cannot reasonably avoid the injury themselves, and that

The costs of the practice outweigh any countervailing benefits of the practice.[14]

Thus, limitations already imposed by Congress, the Supreme Court and the FTC itself ensure that the Commission will not abuse its authority to restrict unfair advertising. Such authority must be preserved so that the FTC can continue to act against advertising that not only damages the public's economic well-being but that endangers the public health.

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[9] *Lorillard, Inc.* 80 FTC 455 (1972).

[10] *Porter and Dietsch*, 90 FTC 770 (1977).

[11] *Heinz W. Kirchner*, 63 FTC 1282 (1963).

[12] *Porter and Dietsch*, *supra*, note 10.

[13] *J. B. Williams Co., 81 FTC 238 (1972)*

[14] "Unfairness: Views on Unfair acts and practices in Violation of the Federal Trade Commission Act" (1980), U.S. Congress, Committee on Commerce, Science and Transportation, Consumer Subcommittee (1980); published as a "Committee Print."

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, D.C., March 19, 1982.

Hon. BOB KASTEN,
Chairman, Subcommittee on Consumer, Russell Senate Office Building, Washington, D.C.

DEAR BOB: As the Consumer Subcommittee of the Senate Commerce Committee continues consideration of legislation reauthorizing the Federal Trade Commission, we urge you to reject any attempt to "clip the Agency's wings" in dealing with unfair and deceptive advertising practices. Fair competition and the future credibility of all advertising depend on a strong FTC presence in this area.

Consumers and advertisers alike benefit from the FTC's efforts with respect to commercial advertising. It would be wrong to curtail them. Rather than limiting the freedom to advertise, the FTC stands out as the leading advocate of the contribution which truthful advertising can make to vigorous competition.

The FTC's Eyeglass Advertising Rule, which eliminated unjustified restrictions on the truthful advertising of eyeglass-related services, has helped save American consumers millions of dollars. And the FTC's Advertising Substantiation Rule, by requiring all advertisers to have in hand reasonable evidence before making specific advertising claims, has been a boon to the vast majority of ethical advertisers who would otherwise be forced to compete against the misleading claims of a dishonest few.

These and similar FTC accomplishments on behalf of consumers and ethical advertisers must not be jeopardized by an overzealous attempt to weaken the Agency. We must not give Carte Blanche to the handful of advertisers who would like nothing more than to keep the FTC from policing unfair and deceptive advertising practices. Yet that is precisely what would happen if current proposals were adopted to force the FTC to prove before bringing suit that, among other things, advertisers knew or should have known the advertisements were misleading.

Mr. Chairman, today when Americans see, hear or read advertisements, they can believe the claims advertisements make. This is due to no small part to the efforts of the Federal Trade Commission. We urge you to take no action which would undermine this critical role played by the FTC in promoting truthful advertising.

Very sincerely yours,

EDWARD M. KENNEDY,
WILLIAM PROXMIRE,
HOWARD M. METZENBAUM,
PAUL E. TSONGAS,
U.S. Senators.

ASSOCIATION FOR THE ADVANCEMENT OF PSYCHOLOGY,
March 24, 1982.

Hon. ROBERT W. KASTEN, Jr.,
Chairman, Consumer Subcommittee, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: We are writing in regard to S. 1984, "A bill to amend the Federal Trade Commission Act to protect the legislative and regulatory authority of the state legislatures, and for other purposes." We understand that you will be considering this bill in March and request that this letter be made part of the record.

The American Psychological Association is the major organization of psychologists in the United States. It is a 65,000-member society "dedicated to the advancement of psychology as a science, as a profession and as a means of promoting human welfare." The Association for the Advancement of Psychology is the major advocacy organization for psychology.

We have previously communicated with this subcommittee on this issue in 1979, 1980, and 1981. We would at this time, like to address several points in the bill under consideration, S. 1984.

The most important issue, we believe, is that some professions are currently in a position to control or monopolize the market for their services (and related services) and are clearly attempting to do so. The most abusive profession in this regard to psychology is the medical profession. Groups of physicians, nonprofit associations of physicians, and corporations controlled by physicians have actively worked to control, restrict or deny the professional practice of psychology by psychologists.

Psychologists are credentialed in all 50 states and the District of Columbia as practitioners of clinical services, are recognized in most federal health-related laws, are members of the faculty in every U.S. medical school, are required by state law to be reimbursed for their services by health insurance companies in 33 states (representing over 80 percent of the U.S. population). Despite a clear market for their services, and recognition of their efficacy by consumers and state and federal governments, organized medicine is unfailing in its efforts to deny access to psychologists by the public. They have acted to prevent granting hospital staff privileges to psychologists, prevent group practice between physicians and psychologists, deny health insurance reimbursement to psychologists at the state and federal levels, and enact "physician supervision" or "physician-only billing" requirements for psychological services.

For example, Blue Shield of Virginia instituted a requirement that psychologists be "supervised" by and billed through physicians for health insurance coverage of their clinical services—in direct contradiction of a Virginia law requiring the direct access of patients to clinical psychologists. In a successful antitrust suit brought by the Virginia Academy of Clinical Psychologists against Blue Shield of Virginia, et al., (624 F 2nd 476 [4th Cir, 1980]), the Fourth Circuit Court of Appeals held that "it is not the function of a group of professionals to decide that competition is not beneficial in their line of work, and we are not inclined to condone anticompetitive conduct upon an incantation of 'good medical practice'. Moreover, we fail to see how the policy in question fulfills the goal. Any assertion that a physician must actually supervise the psychologist to assure the quality of the psychotherapy treatment administered is refuted by the policy itself. The Blue Shield policy provides for payment to psychologist for psychotherapy if billed through any physician—not just those who regularly treat mental and nervous disorders. It defies logic to assume that the average family practitioner can supervise a licensed psychologist in psychotherapy, and there is no basis in the record for such an assumption . . ."

The real purpose of the Blue Shield action, we maintain, was to regain a medical monopoly over the delivery of health services.

The Federal Trade Commission staff recently investigated the many Blue Cross/Blue Shield plans in the United States—an investigation with which our organizations voluntarily cooperated. The FTC staff found clear evidence that the Blues are substantially controlled by the very physicians who submit reimbursement claims. With this knowledge, it is understandable that hyperinflation in health care costs is not likely to be checked by those physicians who are growing rich from inflated charges. Additionally, it is predictable that the consumer of health care services is the one to suffer most, both in economic terms and in health status, from this hyperinflation.

Another organization controlled by physicians is the Joint Commission on the Accreditation of Hospitals (JCAH). It was formed, and is governed, by the American Medical Association, the American Hospital Association, the American College of Physicians and the American College of Surgeons. JCAH has for many years waged a campaign to prohibit non-medical practitioners from competing with physicians in hospitals. They have gone so far as to threaten denial of accreditation to hospitals that have granted staff privileges to clinical psychologists. As the members of the Consumer Subcommittee probably know, JCAH accreditation is a requirement for reimbursement from virtually every private and public health insurance system. This is true despite the fact that JCAH is a private organization, with no mechanism for public redress, Congressional oversight or citizen input. Our organizations have entered a well-documented complaint against JCAH with the Federal Trade Commission. We intend to continue to urge the FTC to investigate our allegations.

Presently, antitrust laws apply generally across the board to all individuals, partnerships and corporations who are engaged in and who reap benefits from our American system of free enterprise. This includes, of course, physicians, psychologists, lawyers, accountants, architects, engineers, and many other providers of services who regard themselves as "professionals", and who are duly licensed as such by their states.

The Supreme Court has repeatedly recognized that antitrust liability does apply when "professionals" engage in anticompetitive practices in violation of the federal antitrust laws. *Golfarb* v. *State Bar,* 421 U.S. 773 (1975); and the *National Society of Professional Engineers* v. *United States,* 435 U.S. 679 (1978).

Section 2 of S. 1984 exempts from FTC purview "practitioners of a profession whose members are licensed and regulated by a state", and "incorporated or unincorporated associatons of state-regulated professions". The theoretical basis for these exemptions is that credentialing of the professions is a state function, and thus the Federal Trade Commission should not interfere.

However, if professionals were to be given a privileged status of immunity from the antitrust laws, such a program would be a bureaucratic nightmare to administer. It would be extremely difficult to draw the line in the determination of what constitutes an appropriate professional for the purpose of antitrust immunity. Many members of the service sector of our economy, such as real estate brokers, funeral directors and others, regard themselves as professionals. Their specialties require advance training and education, and they are subject to state licensure/certification and regulation. Members of these numerous professions would undoubtedly claim that because they are subject to professional codes of ethics and state laws which control their practice, they should be given the same antitrust immunity as might be sought by physicians, psychologists, lawyers and accountants.

More fundamentally, giving special recognition to "professionals," even assuming the term could ever be manageably defined, would create a dual standard that would seriously violate the confidence among our business community in the concept of even-handed administration of justice. To illustrate with just one example, a businessman who has been exposed to years of civil litigation because he exchanged price and cost information on a reciprocal basis with his competitors (see *United States* v. *Container Corp.*, 393 U.S. 333 [1969]) could hardly be expected to understand, and accept as fair, a system of justice that would allow the lawyers and accountants who advised him on antitrust liabilities to act with impunity themselves in anticompetitive fixing of legal or accounting fees. Such a dual standard would be offensive to most American who have been taught to believe in a system of equal justice under law for all.

Section 2 would not only exempt individual professionals, but the national associations through which they act from antitrust law. Historically, trade associations have been fertile ground for both antitrust violations and antitrust litigation. That national trade associations, including professional associations, may establish themselves as non-profit business leagues in order to take advantage of tax treatment under Section 501(c) of the Internal Revenue Code, is certainly no justification for exempting these organizations from antitrust scrutiny simply because the associations themselves are not engaged in business for profit.

We are not talking here about purely charitable corporations such as churches or foundations. Rather, we are talking about professional and business organizations who are acting jointly, through membership associations, to influence public policy, to develop standards for their professions, to obtain economic benefits for themselves, and to shape and control a significant measure of the American economy. It it unsupportable that firms and individuals with significant economic power who are engaged in commercial endeavor for profit in interstate commerce should somehow escape scrutiny because they act jointly through a non-profit membership organization.

Section 3 of S. 1984 precludes the FTC from gathering information, investigating, or prescribing rules affecting "any person, partnership or corporation acting in conformance with applicable state law," and adds the general comment that "nothing in this section shall authorize the Commission to promulgate any rule affecting any State regulated profession, or individual members thereof, or its State or national professional associations." It is interesting to note the use of the following words: "The Commission shall have no authority for purposes of this section to prescribe any rule with respect to *unfair or deceptive acts* or practices in or affecting commerce . . . regulating" the professions. (emphasis added)

The intent of this section is to prevent FTC rules from preempting state laws that interfere with competition or that allow unfair or deceptive acts or practices. The pre-emption of inconsistent state laws by federal laws is well established throughout prior legislative history. The appropriateness of uniformity in certain areas has justified pre-emption. Certainly, when there are no directly applicable federal provisions, then state laws should not be pre-empted. However, when state laws promote (or require) anti-competitive, pro-monopolistic, or anti-consumer actions on the part of professionals, it is entirely appropriate that these laws be investigated and preempted by federal actions.

This section would preclude the Federal Trade Commission from enforcing the antitrust laws even-handedly with regard to both professionals and business corporations, even though the Commission has reason to believe that such groups or business entities have engaged in unfair methods and actions in violations of federal antitrust laws. We believe that such restrictive legislation would be unsound as a matter of public policy. It could only diminish the ability of the federal government to ensure that important areas of the economy are in fact subject to open, free-market competition.

While it is true that many of the key cases involving antitrust laws and professionals have derived from cases developed and prosecuted by the Department of Justices's Antitrust Division, it makes no sense, given the limited resources of that Division and its commitment to enforcement of criminal antitrust cases, to strip another federal agency with many years of expertise and experience from exercising concurrent jurisdiction over civil antitrust violations. Most antitrust cases involving professionals will probably be in the civil area due to the larger role that "rule of reason" analysis plays there. It is reasonable to expect that a substantial amount of the work in this area will and should be accomplished by the Federal Trade Commission, which has special resources, particularly for conducting industry-wide investigations, which the Department of Justice lacks. Moreover, the long-standing and widely-recognized liaison policy between the Federal Trade Commission and the Antitrust Division successfully avoids duplicative proceedings; there is no reason to fear that concurrent jurisdiction would cause any diseconomies or waste.

Perhaps most importantly, if the Federal Trade Commission's jurisdiction is limited, Congress cannot expect that private litigants or state governments proceeding under Section 4 and 16 of the Clayton Act will be able to take up the slack and bring antitrust standards to bear on professionals and professional associations who have engaged in unreasonable restraints of trade. While some of the key cases involving application of antitrust standards to professionals have arisen in the context of private litigation (for example, the *Goldfarb* case), private litigants simply cannot shoulder the burden of what should be a federal government responsibility.

Such litigation has been and often will be brought by excluded members who have not been able to achieve equal economic status with the professionals whose practices have been challenged. Therefore, there usually is a gross disparity in economic resources between the plaintiffs who seek antitrust relief and the entrenched organizations who have engaged in the contested anticompetitive practices.

Because of the expense and the other taxing costs of discovery in civil litigation in the federal courts today, there are very few individuals or groups of individuals who have the resources to litigate an antitrust case through the entire appeals process against a large, well staffed and well financed professional association.

Section 4 of the bill would require the Federal Trade Commission to pay the costs of supplying information preparatory to an investigation. While this seems reasonable with regard to small companies or associations that could be subject to substantial financial injury by the costs of a large-scale investigation, it seems hardly appropriate with regard to all of the FTC's investigations. Large organizations should be able to handle the financial burden. The effect of this section, it would seem, would be to seriously limit the ability of the FTC to undertake investigations of unfair, anti-competitive, and anti-consumer actions—to the serious detriment of the good of the American public.

We oppose Section 5 which would delete the FTC's authority to issue subpoenas, and require that they be sought through a District court. It seems to be the intent of this section to eliminate abuse of the subpoena power and to vest subpoena authority outside of the agency. However, current rules require that one of the Commissioners sign any subpoena that is issued. This change, we understand, has effectively eliminated real abuse in this area.

Court subpoenas would impose the possibility of legal sanctions against non-complying individuals. This is in marked contrast to the reason used to justify this section by some analysts—that individuals who do not comply with an FTC subpoena are subject to "adverse findings" whereby it is presumed that any material not presented would be adverse to the individual not complying. This principle would also hold for a District Court subpoena, with the added possibility of being found in contempt and subject to fines or imprisonment.

Additionally, this section could add significantly to the work load of our court system—a situation that does not seen to be justified or desirable.

Section 6 would redefine an "unfair method of competition or an unfair or deceptive act or practice" as "an act which causes substantial consumer injury that outweighs the benefits derived from such act." In effect, this section would require a cost/benefit analysis before it could be determined that the FTC may act.

Our understanding is that cost/benefit analyses are already normal procedure in consumer protection cases undertaken by the FTC. However, in obvious (per se) violations of the law, it does not make sense to add the cost/benefit requirement. It is our position that the new definition of cost/benefit analysis is more vague and uncertain than the present practice and would not contribute to a clarification of the law.

Section 7 would eliminate the current use of FTC Administrative Law Judges, and require that all FTC actions be undertaken in Federal District Courts. The intent of this section appears to be to prevent any hint of prejudice in the first hearing on any action brought by the FTC. The effect of this section, however, would be to eliminate the special expertise that Administrative Law Judges provide.

Currently, after an Administrative Law Judge considers a case, it can be appealed to the entire Federal Trade Commission—and no communication between the Administrative Law Judges and the Commissioners regarding a case under consideration is allowed. The party may seek further redress at the Appeals Court and on the U.S. Supreme Court. Under the procedures in this section, however, the case moves through only three levels: District Court, Court of Appeals and Supreme Court.

The existing mechanism of two hearings within the FTC structure would appear to offer extra protection for the defendant, offers both parties the benefit of expert administrative judges, and prevents our overburdened court system from having to take responsibility for every case. We do not believe the proposed change is appropriate.

In conclusion, we do not support the provisions of S. 1984. Too much of its effect would be to allow professions and their associations to circumvent valid and valuable law. Too much of its effect would be to prevent the Federal Trade Commission from acting against anti-competitive, monopolistic, and anti-consumer activities. Too little of its effect would be any benefit to the citizens of this country.

In a time when major efforts need to be made to increase free competition among professionals and others, vigilant enforcement of consumer-oriented, pro-competitive laws is an absolute necessity.

We hope these comments are useful in your deliberations. Thank you for the opportunity to present them.

Sincerely yours,

Clarence J. Martin,
Executive Director and General Counsel,
Association for the Advancement of Psychology.

Michael S. Pallak, Ph. D.,
Executive Officer, American Psychological Association.

College of American Pathologists,
Skokie, Ill., March 25, 1982.

Hon. Bob Packwood,
Chairman, Senate Committee on Commerce, Science, and Transportation, Washington, D.C.

Dear Mr. Chairman: On behalf of the members of the College of American Pathologists we would like to take this opporltunity to express our strong support for S. 1984, a bipartisan bill introduced by Senator McClure and other Senators, to amend the Federal Trade Commission Act. The College would like to especially endorse that provision which would exclude the professions from within the jurisdiction of the Federal Trade Commission.

The College of American Pathologists is a non-profit professional organization which represents some 8,900 physicians, who practice the medical specialty of pathology in various settings, including the hospital; the independent medical laboratory; in the academic setting in the various medical schools and teaching hospitals throughout the country; and in a number of other settings which render high quality health care services to our citizens.

Over the past several years, our profession has observed with more than little concern the efforts of the Federal Trade Commission to expand its activities over the daily practices of the medical profession and the services they render to their patients. These relatively new efforts on the part of the FTC undertaken in the name of preserving competition in the health care industry, has only served to raise doubts in the minds of the consumer-patient on the one hand, and to raise issues which tend to disrupt the physician in his daily medical practice.

S. 1984 would provide for an exclusion of those state-regulated professions from the jurisdiction of the Federal Trade Commission. This provision does not provide a general exemption from the anti-trust laws or other remedies available for alleged wrongful actions. Moreover, it should be re-stated that such an exclusion would not establish a new precedent, for the Federal Trade Act now provides outright exemptions for several industry groups, including the banking industry and the common carriers. We strongly feel that the professions are more than adequately being regulated at the state level and that additional authority for the Federal Trade Commission over such activities is unwarranted.

Mr. Chairman, on behalf of all the members of the College, we urge your favorable consideration of these views and urge your support for S. 1984, particularly that provision which would exclude the professions from within the activities of the Federal Trade Commission.

We would appreciate very much the inclusion of this statement in the official printed record of hearings held on March 18 and 19, 1982.

Sincerely,

JAMES D. BARGER, M.D., President.

NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS,
Arlington, Va., March 26, 1982.

Hon. ROBERT W. KASTEN, Jr.,
Chairman, Subcommittee on Consumer, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: On behalf of the National Association of Federal Credit Unions (NAFCU)—the only national organization exclusively representing the interests of credit unions chartered by the federal government—I would like to bring to your attention a matter of concern to the members of this Association.

When the Federal Trade Commission Act was enacted in 1914, banks were specifically exempted from the regulatory and investigative authorities of the newly-created Commission because they were already regulated by the Federal Reserve Board. Savings and loan associations were granted a parallel exemption in July, 1979, by the enactment of Public Law 96-37. Thus, Federal credit unions are the only type of federally chartered depository institution regulated by the Federal Trade Commission.

I respectfully request that you support an exemption for Federal credit unions from Federal Trade Commission jurisdiction similar to the exemption which presently exists for banks and savings and loan associations.

The precedent for exempting Federal credit unions from Federal Trade Commission jurisdiction is well established. In addition, such an exemption would eliminate unnecessary, costly and duplicative regulation of Federal credit unions, which is a stated objective of the Financial Regulation Simplification Act of 1980 (Title VII, Public Law 96-221). NAFCU suggests that the National Credit Union Administration, which is the independent agency of the federal government with primary responsibility for the regulation, supervision and examination of Federal credit unions, should regulate Federal credit unions with respect to consumer protection matters and most areas of antitrust, rather than the FTC.

We presented this proposal in testimony before the Senate Committee on Banking, Housing and Urban Affairs last spring when that Committee held hearings on competition and conditions in the financial system. Also appearing at those hearings were representatives of the National Credit Union Administration and the Federal Trade Commission.

Regarding our proposal to exempt Federal credit unions from FTC jurisdiction, the Honorable Lawrence Connell, then Chairman of the National Credit Union Administration Board, stated:

"Section 18(f)(1) of the Federal Trade Commission Act provides that the Federal Reserve Board has the authority to promulgate similar regulations for banks when the FTC issues a Trade Regulation Rule affecting banking or finance areas. The Federal Home Loan Bank Board was provided similar authority for savings and loan associations. We ask the committee to consider granting the same authority to NCUA, so that Federal credit unions and their members will have the benefit of trade regulations that have been carefully considered by their supervisory agency."

When requested to present the views of the Federal Trade Commission on this suggestion, Ms. Linda Colvard Dorian, Deputy Director of the FTC's bureau of competition, commented:

"The Commission supports a provision similar to that contained in Section 18(f) of the Federal Trade Commission Act, giving the National Credit Union Administration authority to issue trade regulation rules prohibiting unfair or deceptive practices by federally insured credit unions. The same reasoning which led the Congress to adopt this approach for savings and loan institutions insured by the Federal Home Loan Bank Board in Public Law 96-37 appears applicable to credit unions."

Accordingly, the members of this Association believe that there is no valid reason to subject Federal credit unions to Federal Trade Commission regulation. As an association, we are satisfied that the National Credit Union Administration has the necessary regulatory tools to protect the member-owners of Federal credit unions.

We strongly recommend ending Federal Trade Commission rule-making authority over Federal credit unions and eliminating unnecessary and costly duplicative regulation to which Federal credit unions are presently subjected.

I appreciate the opportunity to present the views of the National Association of Federal Credit Unions on this important issue and request that this letter be included in the official hearing record of your subcommittee on the Federal Trade Commission reauthorization. If you would like to discuss this issue further, please do not hesitate to contact me or our director of government affairs, Bill Donovan, at 522-4770.

Sincerely,

MAL NESTLERODE,
Executive Vice President.

THE PROPRIETARY ASSOCIATION,
Washington, D.C., March 30, 1982.

Hon. ROBERT KASTEN,
Chairman, Consumer Subcommittee, Committee on Commerce, Science, and Transportation, Russell Senate Office Building, Washington, D.C.

DEAR MR. CHAIRMAN: The Proprietary Association—the 101-year-old national trade association which represents the manufacturers of nonprescription (OTC) medicines—is pleased to submit, for inclusion in the official Subcommittee record on the Federal Trade Commission authorization and oversight hearings conducted on March 18 and 19, 1982, the statement contained herein.

The FTC Improvements Act of 1980 contained important provisions that are scheduled to expire on September 30, 1982. The temporary provisions that affect the Commission's regulation of commercial speech, which were adopted after careful consideration, should be made a permanent part of the FTC Act. In addition, it is important that certain amendments be made in the Act to guide the Commission's regulatory initiatives in the commercial speech area.

The controversy that preceded the FTC Improvements Act of 1980, and convinced the Congress that changes in the Commission's jurisdiction were needed, focused largely on Commission activities affecting commercial speech. The hearings that resulted in the FTC Improvements Act provided overwhelming evidence of the need to limit the Commission's use of an unfairness rationale to ban truthful commercial speech and of the importance of the Commission's promulgating, at the beginning of any TRR proceeding, the text of the rule it proposes to adopt. The children's advertising proceeding provided the most dramatic and publicized, but by no means the only, illustration of the need for these provisions.

The concerns that were crystallized by the children's advertising proceeding led to the adoption of a moratorium on any new rulemaking initiatives premised on an unfairness theory. That moratorium, which is scheduled to expire on September 30, 1982, should be made a permanent part of the FTC Act. Since the policy considerations justifying a ban on use of an unfairness theory in commercial speech rulemaking extend equally to adjudicatory proceedings under Section 5 of the FTC Act, we also believe that the phrase "unfair * * * acts or practices," appearing in Section 5 of the FTC Act, should be defined expressly to exclude commerical speech—leaving the Commission with well-defined authority to regulate or prohibit commercial speech that is false or deceptive.

Further, in light of the constitutionally-protected status of commercial speech, and of the significant differences in meaning that may derive from the context in which particular commercial speech occurs, we believe that Section 5(m)(1)(B) of the FTC Act should be amended to prevent the Commission from seeking to apply and endorse against persons who were not respondents in the original administrative proceeding.

The hearings that preceded adoption of the FTC Improvements Act of 180 provide more than ample evidence of the wisdom of these recommendations. Although these recommendations may not provide absolute assurance that the regulatory excesses that pre-dated the Improvements Act will not be repeted, they will at least provide significant guidance to the Commission in one of the most sensitive areas of its jurisdiction—the commercial speech area.

None of the recommendations we have made would require, of themselves, suspending or ending the antacid warnings proceeding, which was initiated in 1976 and remains of immediate concern to The Proprietary Association and its members. It should be noted, however, that the antacid proceeding was based in substantial part on an unfairness theory that had been fashioned by the Commission staff—and that the policy considerations justifying a ban on new rulemaking proceedings based on an unfairness rationale apply with full force to the antacid proceeding.

Moreover, the antacid proceeding, like the children's advertising proceeding, was initiated without a proposed rule. The Commission's own presiding officer acknowledged in his report that, as a consequence, "much of the testimony [in the proceeding was] largely unfocused[,] * * * deal[t] largely in theoretical concepts or considerations and, for this reason, poses a problem in attempting to evaluate it for its value to this rulemaking * * *." The presiding officer also stated that, on the basis of the record in the proceeding, the imposition of a "product-specific" warning requirement represented a "bleak prospect."

Since the hearings phase of the antacid warnings proceeding was concluded prior to adoption of the FTC Improvements Act, the provision of that Act requiring the promulgation of a proposed rule at the outset of any TRR proceeding does not technically require the suspension of that proceeding. But, again, the policy considerations underlying the requirement of a proposed rule clearly apply to the antacid proceeding. Indeed, as was emphasized in a colloquy among Senators Ford, Danforth and Warner, who managed the Improvements Act during Senate floor consideration, the Commerce Committee's expectation was that the Commission would "take a close look at the [antacid] proceeding—particularly those problems associated with the failure to propose a rule at the outset of the proceeding."

For all of these reasons, we are hopeful that the Commission will recognize the wisdom of ending the antacid proceeding once it has had an opportunity to consider the issues raised there.

We appreciate this opportunity to present these views and hope that this information will be helpful to the Subcommittee during its deliberations on the Federal Trade Commission.

Sincerely,

JAMES D. COPE, *President.*

NATIONAL ASSOCIATION OF BROADCASTERS,
Washington, D.C., April 2, 1982.

Hon. BOB PACKWOOD,
Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C. 20510

DEAR CHAIRMAN PACKWOOD: I am writing to express the views of the National Association of Broadcasters on issues currently being considered by your Committee concerning the scope of the authority of the Federal Trade Commission over advertising.

NAB's major concern remains with the FTC's roving power to restrict truthful, non-deceptive advertising (the exercise of which was witnessed in the so-called "Kid Vid" proceeding, among others) under the rubric of "unfairness." Congress finally challenged and stopped the FTC's proceeding ahead in "Kid Vid" on the basis of the unfairness standard. As a result of that reduced mandate, the Childrens' Television rule making was terminated—the FTC determined not to go ahead on the basis of their "deception" standard.

NAB agreed with the decision to end "Kid Vid," precisely because those proposals were not capable of proceeding on the basis of the "deception" standard, and thus rightly should not proceed at all. Nor should the rule making ever have been begun. Absent the "unfairness" standard it would not have been. But, taking advantage of the elasticity of the term "unfairness," the FTC saw a green light to apply its values as to what "should be," and in the process aptly was dubbed "the national nanny."

Also caught up in that process were the First Amendment rights to truthful non-deceptive commercial speech of advertisers and broadcasters. It was, and is, the unfairness standard that invited chipping away at these First Amendment freedoms—and, as in Kid Vid, handed the FTC a meat cleaver rather than the kid gloves required when dealing with First Amendment rights.

And the Childrens' Television rule making by no means stands alone as evidence of the danger to free speech occasioned by the "unfairness" standard. The list of governmental attempts to restrict truthful non-deceptive speech includes the rule making on over-the-counter drug claims, the Games of Chance in the Food Retailing and Gasoline Industries rule and the Food Advertising rule making.

It is for these reasons and because of our recent history with FTC over-stepping its mandate from Congress that NAB urges the abolition of the "unfairness" standard for FTC regulation of advertising, both as to rulemaking and case-by-case proceedings.

It is this same concern with heavy handed, overbroad agency regulation which leads NAB to dispute the philosphy and effect of section 5(m)(1)(B) of the Federal Trade Commission Act. It seems to us that it is the hight of government presumptuousness and overreaching to apply to a class of businesses the government structures ordered or agreed to by a single company individually charged by the FTC and individually assessing the options in a particular consent degree or adjudications. NAB urges the repeal of section 5(m)(1)(B).

Respectfully submitted,

Vincent T. Wasilewski.

The National Association of Optometrists and Opticians, Inc.,
Washington, D.C., April 5, 1982.

Hon. Robert W. Kasten, Jr.,
Chairman, Subcommittee on the Consumer, Russell Senate Office Building, Washington, D.C.

Dear Mr. Chairman: On behalf of the National Association of Optometrists and Opticians, Inc., I am submitting the enclosed recent editorial from The Wall Street Journal. This editorial pertains to your recent hearings regarding the Federal Trade Commission ("FTC"), and it corresponds closely to our remarks before your Subcommittee last July. Please, if timely, include this comment by The Wall Street Journal for the record on the FTC authorization hearings and S. 1984. We believe the enclosed merits careful attention by the entire Senate Commerce, Science and Transportation Committee.

Respectfully submitted.

James E. Ritchie, *Counsel.*

Enclosure.

[From the Wall Street Journal, Apr. 2, 1982]

Deregulating the Doctors

We see that the deregulation movement has run into a small case of internal wrangling lately over the issue of how to treat professionals like doctors and dentists. One bunch of self-proclaimed deregulators wants to end the jurisdiction that the Federal Trade Commission now holds over these groups. Another camp of deregulators is fighting to preserve the commission's role. One this one, we are on the side of the Feds.

In the name of deregulation, a bill has been filed in Congress to stip the FTC of its present authority over the trade practices of professions that are already regulated on the state level. But the Reagan administration, so eager to shrink the federal government in most respects, won't go long. In fact the FTC's new deregulating chairman, James C. Miller III, has just testified to Congress that he "fully, strongly and unalterably opposes" the effort. This puts Mr. Miller on the side of the Naderites for a change.

But the reason for Mr. Miller's unaccustomed territorial sensitivity is not very mysterious. If the FTC were to lose power over the professions, they would be left to the exclusive control of state authorities. In principle this would not be a bad idea. But it happens that the history of state control over the professions has been largely a story of protectionism. Time and again professionals have been able to use the cloak of state authority, with its licensing requirements and codes of behavior, to restrict competition and keep others out of their lucrative trades.

The FTC has been moving against this kind of restrictiveness, and has acted to open up the legal, dental and medical fields to advertising by parctitioners. Returning jurisdiction to the states would kill the movement.

In general, it's a good idea to keep the federal goverment out of things; generally, more power to the FTC has meant more punitive and unnecessary regulation. But this time the commission is on the side of the markets. And it bears repeating that the purpose of deregulation is to let the market in, not simply to switch regulatory functions from one jurisdictional box to another.

In fact we should keep this pont in mind during the debates to come over all the current "new federalism" initiatives: A lot of what is going to be walking around disguised as decentralization or deregulation just may, when you take a closer look, turn out to be just the same old protectionism underneath.

OPTICIANS ASSOCIATION OF AMERICA,
April 5, 1982.

Hon. ROBERT W. KASTEN, Jr.,
Chairman, Consumer Subcommittee, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

DEAR SENATOR KASTEN: The Opticians Association of America opposes legislative proposals to grant state regulated professions immunity from the regulatory authority of the Federal Trade Commission. An exemption by stifling competition among providers of optical products and services would harm the more than 124 million Americans who wear eyeglasses and contact lenses. It would create a double standard by affording two groups of sellers of eyeglasses and contact lenses an unfair competitive advantage over a third. And it would undercut the FTC's authority to conduct investigations, enforce existing laws and regulations, or issue rules affecting a substantial segment of the eyewear delivery system.

THE EYEWEAR DELIVERY SYSTEM

An estimated 58.6 percent of the American people wear prescription eyeglasses or contact lenses. Last year consumers purchased 48.5 million complete pairs of eyeglasses. They also bought 7.9 eyeglass lenses, 2.4 million frames, and 5.9 million pairs of contact lenses.

Americans buy prescription eyewear from three major classes of providers: ophthalmologists, optometrists, and opticians. According to a survey conducted by the Optical Manufacturers Association, ophthalmologists accounted for 14.5 percent of the eyeglasses and contact lenses sold in 1979. Optometrists sold 39.2 percent. Dispensing opticians, including large national chains and small independents, sold the remaining 41.8 percent.

Ophthalmololgists and optometrists are licensed in 50 states, the District of Columbia and Puerto Rico and can both prescribe and dispense corrective eyewear. Opticians on the other hand, are licensed in 22 states and unlicensed in 28. They do not examine eyes to determine the need for vision correction or prepare prescriptions for the eyeglasses or contact lenses. Their functions are limited to preparing and dispensing eyewear on the basis of prescriptions written by ophthalmologists or optometrists.

REASONS FOR OPPOSING IMMUNITY FOR STATE REGULATED PROFESSIONS

Ophthalmologists and optometrists examine and prescribe and, in many instances, also sell what they prescribe. Hence opticians oppose legislation that would exempt them from FTC jurisdiction. Such legislation would erect a formidable competitive barrier between them and dispensing opticians. It would mean that ophthalmologists and optometrists who sell eyeglasses and contact lenses, as well as their state associations, would no longer be subject to anti-trust and consumer protection scrutiny and to remedial action by the FTC. They would be free to prescribe and sell subject only to state laws and regulations that are heavily influenced by private associations acting on their behalf. Dispensing opticians, on the other hand, would be subject to state laws and regulations enacted, interpreted and enforced on behalf of their principal competitors and at the same time also be subject to the anti-trust and consumer protection authorities of the Federal Trade Commission.

All three classes of providers of optical products should be subject to the same rules and be treated equally in the marketplace. The dispensing of eyeglasses and contact lenses is a sale, no matter who does it, and as such continue to be subject to regulatory scrutiny when required by the Federal Trade Commission.

We believe the Federal Trade Commission has exercised its anti-trust and consumer protection authority responsibility and in the best interests of consumers of eyeglasses and contact lenses. In 1962, for example, the FTC promugated Trade Practice Rules for the Optical Products Industry. These rules defined the dispensing of prescription eyeglasses and contact lenses as a sale when done by ophthalmologists, optometrists or opticians. These rules also defined a variety of acts and practices deemed to violate state and Federal laws governing advertising, pricing, payments and credit practices. They provided useful guidance to industry members.

The FTC has brought suit to protect consumers against advertising abuses in the eyeglasses field. (See *Tashoff* v. *F.T.C.* 437 F. 2d. 707 (1970.))

More recently the FTC mandated a prescription release requirement (sustained by the United States Court of Appeals for the District of Columbia Circuit) as part of its Eyeglasses I trade regulation rule.

The prescription release rule requires ophthalmologists and optometrists to give their patients their prescriptions immediately after examining their eyes. This helps to insure that consumers will be able to obtain prescribed eyewear from a provider of the consumer's choosing. It is a prerequisite for competition among providers of prescription eyewear. In upholding the prescription release provisions of the Eyeglasses I rule, the court cited the American Medical Association's longstanding position that . . . "a patient is entitled to a copy of his or her prescription and to have that prescription filled wherever he or she chooses." The court also concluded that "the (rulemaking) record contains considerable evidence that disclaimers have been used (by ophthalmologists and optometrists who sell eyeglasses) to discourage comparison shopping, to mislead consumers as to the locus of liability for unsatisfactory ophthalmic goods and services, and to frighten consumers into purchasing ophthalamic goods and services from the refractionist."

Without the FTC's prescription release requirement, ophthalmologists and optometrists who sell what they prescribe can easily deprive consumers of the opportunity to purchase prescribed eyewear from opticians who are competing among themselves as well as with other sellers of ophthalmic goods and services.

Because consumer access to prescriptions powers the engine of competition among the three groups of providers of eyeglasses and contact lenses, the prescription release rule is meaningless unless it is enforced. If Congress exempts ophthalmogists and optometrists who sell eyeglasses and contact lenses from the applicability of the prescription release rule or takes other action which prevents the FTC from enforcing the rule, competition will be sharply reduced to the detriment of the more than 124 million Americans who wear eyeglasses and contact lenses.

In addition the Federal Trade Commission is currently investigating other anticompetitive restrictions on various providers of ophthalmic goods and services. This investigation and related FTC efforts to indentify and take action against other abuses in the industry should be allowed to continue.

In summary, the Opticians Association of America opposes enactment of legislation that would shield ophthalmologists and optometrists who sell eyeglasses and contact lenses from the anti-trust and consumer protection authority of the Federal Trade Commission. Such legislation would create a double standard under which these two classes of providers would be freed from statutes and regulations governing other sellers of eyeglasses and contact lenses. Neither competition in the optical products industry nor the best interests of consumers would be served by enactment of legislation to exempt these professions.

Sincerely,

J. A. Miller, *Executive Director.*

The State of Wisconsin,
Department of Justice,
Madison, Wis., April 7, 1982.

Hon. Robert W. Kasten, Jr.,
U.S. Senator, Senate Office Building, Washington, D.C.

Dear Senator Kasten: An array of proposals has recently surfaced to alter through expanded statutory definition the proscriptions of "unfair and deceptive acts or practices" in section 5 of the FTC Act. I have followed with interest the recent hearings before the Committee on Commerce, Science and Transportation of the United States Senate and the recent reported statements of FTC Chairman James C. Miller, III on this topic.

The fallout from such changes would have serious consequences on Wisconsin's efforts to control consumer fraud. While not being expressly bound to FTC precedent, Wisconsin has long relied on the guidelines and case law developed at the federal level to help enforce its unfair and deceptive trade practices laws (secs. 100.20(1) and 100.18(1), Stats.). These statutes are enforced almost exclusively through the state courts rather than administratively like the FTC.

State courts have had little problem applying the concepts of unfairness or deception to the ever changing and seemingly limitless types of fraudulent business conduct. A definitive body of case law has developed which clearly outlines the parameters of unacceptable business conduct. By now attempting precise statutory definition, this case law would become obsolete and a free-fire zone to probe and test the new definitions would be created. Instead of injecting certainty and guidance into this area, just the opposite result would be achieved.

The states are assuming a more active role in protecting their citizens from consumer fraud. At a time when federal policy appears to encourage a larger state role, changes to the FTC Act which would jeopardize state level enforcement should be avoided.

Sincerely yours,

Bronson C. La Follette,
Attorney General.

National Retail Merchants Association,
Washington, D.C. April 7, 1982.

Hon. Robert W. Kasten, Jr.,
Chairman, Subcommittee on Consumer Affairs, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

Dear Chairman Kasten: The National Retail Merchants Association ("NRMA") is pleased to provide its views on certain issues related to pending legislation to amend the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. §§ 41 et seq. NRMA's comments will focus primarily on the issues concerning the Commission's jurisdiction to address "unfair" and "deceptive" acts or practices, and the Commission's authority to assess civil penalties for violations of cease and desist orders under Section 5(m) of the FTC Act, 15 U.S.C. § 45(m), and will briefly discuss other related issues concerning the FTC's exercise of its statutory authority. NRMA requests that this communication become a part of the record of your hearings on the FTC Act.

NRMA is a voluntary, non-profit trade association whose over 3,500 members operate more than 35,000 department, chain and specialty stores throughout the nation. NRMA's members have an aggregate annual sales volume in excess of $95 billion and employ over 2.5 million workers. Approximately three-fourths of NRMA's members are small businesses, with annual sales of less than $1,000,000 each. NRMA's members are subject to regulation by the FTC and are therefore vitally interested in the scope of the agency's authority.

While NRMA believes that the FTC has important functions to fulfill in fostering competition and protecting consumers, certain abuses of its statutory power have rightfully sparked the call for a review of the scope of the agency's authority. NRMA thus hopes that an improved and streamlined agency, rather than an emasculated one, will emerge from this review process. At the outset, however, NRMA urges Congress to take care to guard against this review process turning into a forum dominated by special interest groups airing their particular views. In NRMA's opinion, the 1980 oversight hearings were marred by such special interest groups, which pressed for a variety of specific restrictions.

NRMA therefore objects to the provisions of S. 1984 that would exempt "professionals" from the FTC's jurisdiction, a suggestion that clearly reflects one special interest group's reaction to the increasing attention the FTC is paying to such areas as health care and legal services. NRMA fails to see why professionals should qualify for special treatment or should be immune from challenge if they engage in such practices as false advertising or cartel behavior. Health care and other professional services are of increasing importance to the consumer and the economy. NRMA believes that the public interest is furthered by FTC efforts designed to free up the marketplace and enable consumers to make reasoned purchasing decisions.

The fact that such professionals may be licensed or othewise subject to state regulation is no reason to exempt them from the FTC's jurisdiction. The FTC has not challenged any legitimate regulation intended to ensure that consumers receive competent care but has instead focused on traditional anticompetitive practices, false advertising, and regulatory restrictions on truthful advertising and competitive behavior. These are appropriate areas for FTC investigation and, if warranted, challenge. In short, NRMA believes that it would be a mistake for Congress to insulate professionals and their activities from scrutiny by an impartial agency whose mission is to protect consumers and competition. Instead of focusing on the special interests of particular groups, including professionals such as doctors and lawyers, NRMA believes that it would be more beneficial for Congress to focus on generic questions relating the FTC's authority.

Unfairness and Deception.—NRMA continues to be concerned with the breadth of the Commission's jurisdiction over "unfair or deceptive acts or practices." [1] In particular, the expansiveness of the term "unfair" has increasingly become a focus of dissatisfaction over the past years, due to the perception that the Commission was bent on stretching the meaning of "unfairness" as far as possible. Instead of limiting its reach to practices that offended established public policy and resulted in demonstrable harm, the FTC was apparently trying to use its "unfairness" authority as a tool for social reform. Its efforts—particularly in the children's advertising field—earned the agency the nickname of "National Nanny". As a result, special legislation was needed to stop the FTC from basing its proposed rule concerning advertising directed to children on amorphous unfairness grounds.

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[1] NRMA also believes that Congress should soon study the scope of the FTC's authority over "unfair methods of competition." Although this language was originally interpreted consistently with the major thrust of antitrust theory, in recent years the FTC has indicated that it is not bound by traditional antitrust notions.

Business needs firm guidance concerning the boundaries of unfairness. While this issue is not new, it is of mounting importance, in view of the FTC's increased reliance on its unfairness jurisdiction as a basis for challenge independent of its jurisdiction over deceptive practices. Further, mounting concern that proscribing "unfair" practices may impinge on a company's First Amendment rights highlights the need for giving more concrete definition to the term.

As guidance on the scope of the term "unfair", the FTC has often pointed to the Supreme Court's citation, in *FTC* v. *Sperry & Hutchinson*, 405 U.S. 233 (1972), to a broad FTC articulation of its views on unfairness. In that case, the Supreme Court referred to the criteria set forth in the FTC's Statement of Basis and Purpose, Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8355 (1964):

"(1) Whether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been established by statute, the common law, or otherwise—whether in other words, it is within at least the penumbra of some common law, statutory, or other established concept of unfairness; (2) whether it is immoral, unethical, oppressive, or unscrupulosu; (3) whether it cause substantial injury to consumers (or competitors or other businessmen)."

These criteria are of little practical assistance, since almost any practice with tangential undesirable effects could fit within this framework. In an acknowledgement of the need for greater clarification, in December 1980, the Commission issued a letter explaining that it would consider practices which result in unjustified consumer injury to be unfair. According to the Commission, such injury must satisfy three tests: "It must be substantial; it must not be outweighed by any countervailing benefits to consumers or competition that the practice produces; and it must be an unjury that consumers themselves could not reasonably have avoided." Letter to Hon. Wendell H. Ford and John C. Danforth from Federal Trade Commission, December 17, 1980, p. 5. This clarification of the standards for unfairness provides certain quantifiable criteria which give business welcome guidance, yet preserve the flexibility necessary if the "unfairness" concept is to remain adaptable to changing practices.

In its March 5, 1982, letter to this subcommittee and Senator Packwood, the Commissioner suggested that Section 5 be amended to incorporate these standards. NRMA appreciates the FTC's responsible recommendation and thinks that Congress should act on it.

Accordingly, NRMA believes that Section 5(a) of the FTC Act should be amended to prohibit:

"Unfair or deceptive acts or practices in or affecting commerce, so long as those practices directly cause or may forseeably result in substantial injury to consumers which is not reasonably avoidable by consumers themselves and is not outweighed by countervailing benefits to consumers or competition."

This formulation embodies the principle criteria the Commission has acknowledged as bearing on unfairness.[3]

Most importantly perhaps, this formulation would ensure that the prime consideration is whether a practice results in substantial consumer injury. Consumer injury was the focus when, in 1938, Congress amended Section 5 of the FTC Act to add "unfair or deceptive acts or practices" to the prohibition against "unfair methods of competition". Thus, as the Committee Report to the House of Representatives stated:

"The [Wheeler-Lea] amendment makes the consumer, who may be injured by an unfair practice, of equal concern before the law with the merchant or manufacturer injured by the unfair methods of a dishonest competitor." H.R. Rept. No. 1613, 75th Cong. (1938).

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[3] NRMA believes that these standards are only relevant to determining deception, because a representation should be considered deceptive or misleading only if there is reason to believe that consumers relied on the misrepresentation and injury thereby resulted.

The Commission has often ignored this clear Congressional intent that Commission action be prompted by consumer injury. Congress should take this opportunity to put the FTC back on the right track to ensure that substantial injury involving economic or monetary harm is the cornerstone of the FTC action.

Further, it is appropriate to require the FTC to consider the costs and benefits of a particular practice in analyzing whether it is unfair or deceptive. The suggested amendment would not require a rigid quantitiative cost/benefit analysis, but would require consideration of whether the practice challenged as unfair or deceptive actually benefits competition or society and whether any undesirable effects are reasonably avoidable by the consumer. These considerations are appropriate measures for testing whether a particular act or practice should be deemed unfair or deceptive under Section 5. NRMA therefore joins the FTC in asking Congress to amend Section 5 in the appropriate manner.[3]

Moreover, in the deception area, Congress should instruct the FTC that the proper standard for measuring whether an act or practice is deceptive is whether it is likely to mislead consumers acting reasonably under the circumstances.[4] In the past, the FTC has too often relied on its naked "expertise" to discern the meaning of a representation and, as a result, has occasionally construed advertisements as making claims that few if any reasonable consumers would take away from the materials.[5]

In applying this standard to allegedly deceptive claims, the FTC should heed the practice of courts construing advertising challenged as deceptive under Section 43(a) of the Lanham Act, 15 U.S.C. §1125(a). In these comparative advertising cases, courts have generally distinguished between claims that are "false on their face" and implied claims, the falsity of which depends on how they are understood. The falsity of the "false on their face" claims is readily ascertained; survey evidence revaling consumer perception is, however, generally required before the falsity of an implied claim is established. See, e.g. *American Brands, Inc.* v. *R. J. Reynolds Tobacco Co.*, 413 F. Supp. 1352, 1356-7 (S.D.N.Y. 1976). In any event, the FTC should have sufficient grounds for believing that reasonable consumers to whom the advertising is directed would derive the untruthful message from the advertising and would rely, to their injury, on it.

The FTC's advertising substantiation program raises a related issue concerning the basis for the FTC's efforts to ascertain whether a company has sufficient substantiation for its claims. Instead of arbitrarily selecting general kinds of claims for substantiation review—as often seems to have been the practice—before launching an investigation, the FTC should have reason to suspect that a claim cannot be substantiated and that significant economic injury resulted from the lack of substantiation. Adopting such a standard would guard against companies being subjected to groundless probes into their substantiation, at much cost to the companies and the FTC and with little or no countervailing benefit to the public. Those of NRMA's members who were asked to substantiate their "satisfaction guaranteed" policies question whether the FTC would have begun its inquiry, which was closed with no action taken in September, 1981, under this standard.

Civil penalties.—The Commission's current broad authority to seek civil penalties is another major concern of NRMA's. Of particular worry is Section 5(m)(1)(B), 15 U.S.C. §45(m)(1)(B), which authorizes the FTC to seek civil penalties from a company that engages in practices declared unfair or deceptive in another company's order, so long as the second company has been put on "actual notice" of the order—even if the second company was not a party to the proceeding that resulted in the order.

NRMA has continually had serious reservations about the constitutionality of Section (5)(m)(1)(B), as it effectively results in promulgation of industry-wide rules without affording all possibly affected parties the opportunity to comment or participate in the proceeding.[6] Section (5)(m)(1)(B) would therefore seen to violate the due process guarantees of the Constitution.[7] It does not even afford potentially affected companies the minimal notice and comment protections the Administrative Procedure Act, 5 U.S.C. § 551 et seq., requires before an agency can issue a rule. Companies should not be subject to liability for substantial civil penalties if they have no say in the formulation of the rule that they are purportedly violating. NRMA therefore believes that Section (5)(m)(1)(B) should be repealed.

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[3] NRMA opposes any suggestion that Congress compile a list of specific "unfair" practices. Such an approach would eliminate all flexibility in the term "unfair" and would prohibit the FTC from seeking to halt newly devised practices which, although not on the list, are plainly repugnant to public policy and result in significant consumer injury.

[4] This formulation is based on the suggestions of Timothy J. Muris, the current Director of the Bureau of Consumer Protection, as set forth in his memorandum of March 25, 1982 to Chairman James C. Miller.

[5] See, e.g., *Kroger Co.*, 3 CCH Trade Reg. Rep. ¶ 21,887 (1981); *Ford Motor Co.*, 87 F.T.C. 756 (1976).

[6] The FTC's practice has been to send to members of various industries summaries and copies of FTC cases, thereby purportedly putting the companies on notice of the cease and desist orders.

In a related area concerning the amount of civil penalties that can be assessed for a violation of an order, NRMA believes that the statute should define more clearly the meaning of "violation" and should place some cap on a company's potential liability. Sections 5(1) and 5(m) of the FTC Act now state that a company may be assessed up to $10,000 for each violation of a cease and desist order or trade regulation rule. The term "violation" has been construed to mean each piece of mailed matter, *United States* v. *Readers Digest Assn.*, 662 F.2d 955 (3rd Cir. 1981), cert. denied, — U.S. — (Jan. 18, 1982), or each broadcast of a commercial, *United States* v. *J. B. Williams Co.*, 354 F. Supp. 521 (S.D.N.Y. 1973), aff'd in part, rev'd in part, 498 F.2d 414 (2d Cir. 1974). NRMA believes that such interpretations are erroneous and unfair, as they subject an advertiser to potential liability far in excess of a reasonable penalty for a transgression of an order. To make the statute more equitable, Section 5 should be revised to provide that a "violation" consists of all acts of a similar nature undertaken as part of a single transaction or campaign.

Further, a limit should be put on a company's possible monetary liability for civil penalties. In other contexts, such as the Consumer Product Safety Act,[8] Congress has placed a ceiling on a company's potential liability, apparently in recognition of the fact that open-ended liability can be totally unrelated to the seriousness of the violation charged. The FTC Act should therefore be amended to provide that a company can be assessed no more than $500,000 in civil penalties for any related series of violations. This figure is not inconsequential but will guard against such excessive civil penalties as the $1.7 million assessed recently against Readers Digest.

In NRMA's view, the FTC's authority to seek civil penalties for violations of the Fair Debt Collection Practices Act and the Equal Credit Opportunity Act and their implementing regulations should also be restricted. These statutes currently provide that they may be enforced as trade regulation rules, so that the FTC can use its authority under Section 5(m)(1)(A) to procure civil penalties for violations. Thus, the FTC need not proceed by adjudication. as it must to obtain cease and desist orders for violations of other statutes in the credit area, such as the Truth in Lending Act and the Fair Credit Reporting Act. As a result, companies are exposed to potential liability for substantial civil penalties, even for very technical violations of rules that are incapable of easy interpretation and for violations that have nothing to do with the fundamental purposes underlying the statutes. This civil penalty authority gives the staff a powerful leveraging tool, and companies faced with the threat of $10,000 a day in penalties for purely technical violations are more liable to agree to consent orders that would be unthinkable were the cards more evenly stacked. To eliminate this inherent unfairness and to bring the Fair Debt Collection Practices Act and the Equal Credit Opportunity Act into closer conformity with other acts in the credit area, they should be amended to eliminate the FTC's power to seek civil penalties for violations of the statutory provisions or implementing regulations. These statutes already aequately deter noncompliance by providing civil actions and administrative enforcement to remedy violations.

Explicit Defenses.—In addition, the FTC Act should be amended to afford companies certain specific defenses. At the moment, the FTC Act is a one-way street, affirmatively defining the FTC's authority but basically silent on the issue of defenses available to companies whose practices are challenged. NRMA believes that it would be equitable for the FTC Act to contain certain specific defenses. In particular, the FTC Act should be amended to provide that it is a complete defense to an FTC challenge that a practice has been completely abandoned prior to initiation of a formal investigation or that a company has reasonably relied on materials provided by a supplier.

A defense of abandonment would amount to an express recognition that a company should not be penalized for past practices it has halted. The FTC has on occasion proceeded zealously against terminated practices, on the theory that they must prevent any possibility of recurrence. If a practice has been abandoned, however, it is unjust to dredge it up from the past and impose on a company an order relating to practices long since forgotten. NRMA suggests, however, that the availability of the defense depend on voluntary cessation before the FTC launches a formal investigation, to guard against a company's ability to manipulate the defense by ending a compaign in response to anticipated FTC action.

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[7] The only court to have considered this issue upheld the constitutionality of Section (5)(m)(1)(B), in part because the government conceded that a defendant would have the right to raise in a civil penalty action the question of whether the FTC's prior determinations are legally sustainable interpretations of Section 5. *United States* v. *Braswell, Inc.*, 1981-2 CCH Trade Cases ¶64,325 (N.D. Ga. 1981). If Section (5)(m)(1)(B) is retained, it should be amended to remove all doubt on this issue.

[8] See 15 U.S.C. § 2069(a).

Amending the FTC Act to add a specific defense concerning reasonable reliance on a supplier's material would acknowledge business realities and clarify the confusion created by the Seventh Circuit's decision in *Porter & Dietsch, Inc.* v. *FTC*, 605 F.2d 294 (7th Cir. 1979), cert. denied, 445 U.S. 950 (1980). In that case, a retailer was held liable, along with its supplier, for misrepresentations contained in materials prepared by the supplier, despite the fact that the retailer had no knowledge that the claims were false. In holding the retailer liable, the court took the position that Section 12 of the FTC Act—which pertains to food, drug, or cosmetic advertising—places strict liability on all disseminators of such advertising. NRMA's members were understandably concerned by this holding, which seems to assume erroneously that retailers are as familiar with the characteristics of the products they handle as is the product's manufacturer. Congress should restore the equilibrium and make sure that only the party that initiated the misrepresentation is held liable.

Conclusion.—In conclusion, NRMA hopes that this review process will result in Congress' sending the FTC a clear message concerning the scope of the agency's authority. The message should include a reminder that Section 5, while a broad grant of power, should not be used as a band-aid to patch what the FTC perceives to be inadequacies in certain specific statutes, particularly in the credit area. To address credit-related issues, Congress has enacted several laws, such as the Fair Credit Billing Act and the Truth in Lending Act, which require those subject to their provisions to undertake certain actions. Typically, these acts give rulemaking authority to the Federal Reserve Board, which issues very detailed and specific implementing regulations, and enforcement authority to several agencies, including the FTC.

The FTC, however, has been attempting to use Section 5 to require companies to make certain disclosures or undertake affirmative duties beyond those required by these specific acts. In view of these acts' specificity and of their grant of substantive regulatory authority to another agency, the FTC's actions are thwarting Congress' intent. In contrast to those cases upholding the FTC's authority to use Section 5 to close "loop-holes" in other statutes, e.g., *Grand Union Co.* v. *FTC*, 300 F.2d 92 (2d Cir. 1962), the FTC's recent activities in the credit area amount to engrafting additional duties on top of those mandated by Congress or the Federal Reserve Board. The FTC is thus improperly usurping Congress' and the Federal Reserve Board's substantive authority. NRMA believes it would be appropriate for Congress to remind the FTC that it should not use Section 5 as a "gap filling" measure to upset a careful framework established by Congress.

NRMA appreciates this opportunity to submit its views on the scope of the FTC's authority and powers and hopes that these comments will be helpful to Congress.

Respectfully submitted,

VERRICK O. FRENCH,
Senior Vice President, Director of Governmental Affairs.

FEDERAL TRADE COMMISSION,
Washington, D.C., April 9, 1982.

Hon. SLADE GORTON,
U.S. Senate, Committee on Commerce, Science, and Transportation, Washington, D.C.

DEAR SENATOR GORTON: This letter is in response to your March 24, 1982, inquiry requesting my views concerning the reauthorization of the Federal Trade Commission ("FTC"). I have outlined my views below and have attached a copy of a Statement I delivered on April 1, 1982, to the House Subcommittee on Commerce, Transportation and Tourism. That Statement addressed, in more detail, the FTC's: (1) jurisdiction over the professions; (2) consumer unfairness authority; and (3) power to policy deceptive practices. I have also attached a copy of my previous Statement to your Committee on July 15, 1981, discussing FTC investigations and law enforcement activities relating to the professions.[1]

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[1] The July 15 statement is printed in the record of the Consumer Subcommittee hearings on "FTC Activities Concerning Professionals" (Serial No. 97-59).

On antitrust and related issues, I am presently opposed to any change in the FTC's jurisdiction over "unfair methods of competition," particularly those proposals recently advanced by the National Association of Manufacturers and the Chamber of Commerce. While I may have differed with the wisdom of some past individual cases, I believe the Commission can play a unique role in the antitrust area. In particular, the Commission's economic expertise and adjudicative powers provide it with the ability to shape the contours of antitrust policy in a way that can be helpful to the business community as well as the courts. I believe that the importance of the Commission in the antitrust arena will only increase in the years to come as we are presented antitrust issues of increasing complexity and economic import.

I am also firmly opposed, in principle, to the exemption of special interest groups from the Commission's jurisdiction. The Commission has repeatedly emphasized that it will proceed with great caution in considering whether to propose preemptive rules under its consumer unfairness authority. As for the antitrust side of our jurisdiction, there appears to be absolutely no basis for exempting a large sector of the economy from antitrust scrutiny by an agency that has developed a considerable amount of expertise in health care and other professional areas. There are certainly no overriding issues of federalism in the antitrust arena that would make it inappropriate for the Commission to become involved in these markets. To the contrary, the Commission can complement the traditional licensing functions of the states by encouraging innovative, cost-reducing forms of competition. Instead of adding to regulation, the Commission's role is designed to facilitate the removal of unnecessary privately imposed regulation. My views on this subject are more fully elaborated in the attached Statements.

However, as to the Commission's consumer protection authority, I believe there is room for additional Congressional guidance at this time. The most universal complaint about the FTC's unfairness jurisdiction is that it lacks clear definition and is too susceptible to subjective interpretation. Therefore, in December, 1980, the Commission unanimously issued a Policy Statement delineating the criteria that the Commission would consider in deciding whether a particular business practice was unfair. I share the Chairman's view and that of a majority of the Commission that it would now be useful for the Congress to incorporate the specific standards set forth in the Policy Statement into Section 5 of the FTC Act. In my opinion, such legislation would not only provide useful guidance to the business community but also would clarify and enhance the Commission's authority in this regard.

I do not, however, support an exemption for the advertising industry from the Commission's unfairness jurisdiction, although I believe that deception should be the Commission's primary standard for judging advertising, subject, of course, to the constitutional restraints of the First Amendment. Congress should not make advertising immune from meeting the unfairness test of Section 5 of the FTC Act, particularly where substantial consumer injury has resulted.

In contrast to my views on the need to clarify the FTC's unfairness authority, I am presently not persuaded that there is a need to further define deception in the context of Section 5 of the FTC Act. While I would strongly support an effort to reexamine the Commission's internal policy in this area. I believe that the existing law relating to deception is sound and well understood. My views on both unfairness and deception are also discussed in more detail in my April 1, 1982 Statement.

I would also like to make several brief comments on some procedural changes that have been proposed. First, S. 222 proposes that a $1,000,000 cap be imposed on civil penalty assessments for a "related series of violations" of a Commission order or rule. I am opposed to this proposal because it would reduce the incentive for firms to minimize or stop illegal practices and it would take away the discretion of the courts in imposing the appropriate remedy in a particular situation.

Second, proposals have been advanced to repeal of Section 5(m)(1)(B) of the FTC Act, which authorizes the Commission to seek court ordered civil penalties for violations of the FTC Act done "with actual knowledge that such act or practice is unfair or "with actual knowledge that such act or practice is unfair or deceptive . . ." I am opposed to the repeal of Section 5(m)(1)(B). In 1975, Congress specifically strengthened the Commission's authority to seek civil penalties because of its judgment that a cease and desist order may not be a sufficient remedy or deterrent in all situations. I am unaware of any evidence since Section 5(m)(1)(B) was enacted, of Commission abuse in seeking civil penalties in any particular case or of any abuse by the federal courts, which ultimately determine the appropriations and amount of civil penalties. In addition, respondent firms have ample opportunity to litigate the legality of their actions in these proceedings. *See U.S.* v. *Braswell, Inc.*, No. C81-558A (N.D. Ga. 1981), reported at CCH Trade Cases §64,325 (1981). Therefore, I believe that a legitimate case for repeal of this important remedy provision cannot be made.

Finally, I join my fellow Commissioners in supporting Chairman Miller's initiative to make the Commission's cease and desist orders effective sixty days after service, unless stayed. At present, the Commission's cease and desist orders become effective only if no petition for review is filed. If review is sought, the effective date of the order must await decision by the Court of Appeals and, in some cases, the Supreme Court. Therefore, a respondent can currently continue to engage in conduct, often for many years, that the Commission has determined to be unlawful, unless extraordinary ancillary relief is granted by the Court of Appeals. Thus, the status quo may encourage frivolous and unfounded appeals, which clearly are not in the public interest. Therefore, for these reasons, I urge you to support Chairman Miller's initiative to remedy this problem and grant the Commission's cease and desist orders the same force and effect accorded other federal agencies.

I have appreciated this opportunity to share my views on the FTC's reauthorization with you, and will be pleased to answer any additional questions you and other members of your Committee may have.

Sincerely yours,

David A. Clanton, *Commissioner.*

Enclosures.

PREPARED STATEMENT OF DAVID A. CLANTON, FEDERAL TRADE COMMISSIONER

I appreciate the opportunity to discuss the Commission's reauthorization. I will limit my remarks to three issues: (1) FTC jurisdiction over the professions; (2) the Commission's consumer unfairness authority; and (3) its power to police deceptive practices. Before proceeding, however, I would like to emphasize my strong concurrence with the Chairman's desire to have Congress focus its attention on generic issues of FTC policy rather than narrow, special interest concerns. Although I may disagree with the Chairman on a few issues, such as whether a legislative redefinition of deception is needed, I share his view that the Commission's basic substantive authority under Section 5 of the FTC Act should not be immune from careful scrutiny.

PROFESSIONS

I believe that it would be a tremendous mistake to exempt professional organizations, however defined, from FTC jurisdiction. Although couched in terms of federalism and quality-of-care issues, the push for such legislation by medical, legal and other groups is nothing more than a thinly disguised ploy to gain exemption from basic antitrust and related consumer protection laws.

I have submitted a Statement to you today which I delivered to the Consumer Subcommittee of the Senate Commerce Committee last summer outlining in detail the specific focus of the Commission's law enforcement activities in the professional area. Therefore, I will direct my comments today to some of the arguments you have heard from those seeking exemption from the Commission's antitrust jurisdiction.

It is, of course, clear that state regulation of the professions serves many legitimate ends, including protection of the public from fraudulent or incompetent practitioners. The Commission has no desire to control quality of care or to substitute its own licensing scheme for that of the states or localities. What the Commission is interested in is determining whether public and private regulation unnecessarily restricts competitive behavior or consumer choice. In essence, the current debate really focuses on two distinct issues: (1) whether the Commission should have the authority to preempt state law in certain circumstances, and (2) the broader question whether the Commission should retain any authority to address anti-competitive and anti-consumer practices engaged in by the professions.

As to the first issue, the Commission has clearly indicated that it will proceed very cautiously in considering enforcement action directed toward state rules or regulation. In the only instance where the Commission pursued rulemaking,[1] its action was based on solid economic evidence of consumer injury. Moreover, the Commission's eyeglass rule followed closely on the heels of Supreme Court decisions striking down bans on the advertising of prescription drugs and routine legal services.[2] I am confident that the Commission would not step forward in other areas involving these delicate federalism concerns unless it were strongly convinced that the regulations under scrutiny produced substantial consumer injury and had little or no countervailing public benefits. In any event, this very limited issue hardly justifies a blanket legislative exemption for all private activity by professional organizations.

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[1] 16 CFR 456, June 2, 1978; Am. Optometric Ass'n v. F.T.C., 626 F.2d 896 (D.C. Cir. 1980) (D.C. Court of Appeals upheld rule's requirement that sellers provide consumers with copies of their prescription, but remanded the portion of the rule relating to state advertising requirements for further Commission consideration.)

As for the second, broader issue, I cannot conceive of any reason why the professions should receive special interest treatment insofar as the FTC is concerned. If the intent is to have only one antitrust agency dealing with the professions, it seems particularly anomalous to eliminate the FTC, since over the last decade the Commission has been the most active federal enforcement presence in the field and has developed a great deal of expertise and sensitivity about issues concerning the professions. Moreover, one of the Commission's distinctive features is its capability both to conduct in-depth analyses of complex business and economic considerations and to integrate these factors into a legal framework. It is precisely this unique capability that is needed to effectively address the difficult competitive and consumer issues involving the professions.

Clearly, it is beyond dispute that the antiturst laws apply to the professions. Therefore, unless Congress is prepared to eliminate the Commission's antitrust authority entirely, which would be a great mistake, I see no principled basis for treating the professions differently under the antitrust laws than any other group of citizens. Nor was applicability of the antitrust laws to the professions set aside by the Supreme Court's action last week which affirmed, by an equally divided Court, the Commission's decision to overturn the American Medical Association's ban on advertising by physicians.[3] Only two questions were before the Court: (1) whether AMA, as well as its affiliated state and local medical societies, was "organized to carry on business for [the] profit . . . of its members . . .," within the meaning of Section 4 and Section 5(a)(2) of the Federal Trade Commission Act,[4] and (2) whether the Commission should have issued an order against the associations in light of changes which those organzations made to their codes of ethics after the Commission issued its complaint in 1975. Notably, the issue of liability was not before the Court. The AMA specifically did not contest the Commission's finding that the Association's pre-1976 advertising restrictions and violated the antitrust laws; rather, AMA sought only to overturn the decision solely on grounds that the illegal practices had been abandoned and that the Section 4 exemption was applicable.[5]

In its decision, the Commission acknowledged the valuable role the AMA could continue to play in policing deceptive advertising. Indeed, the AMA order specifically permits the national, state and local medical societies to regulate deceptive or unsubstantiated advertising under criteria similar to that applied by the Commission itself under Section 5 of the FTC Act. Therefore, given the current debate about the reach of the Commission's deception authority, it can hardly be said that the AMA order is unduly restrictive. It is also notable that the AMA chose to bring its ethical standards into closer conformity with the Commission's order while this case was still on appeal before the courts. We have received no evidence that this change has prevented the Association from taking appropriate action against nontruthful advertising by member physicians. A similar order governing the American Dental Association for the past two years also illustrates that the Commission has provided ample latitude for reasonable and effective self-regulation.

Therefore, whether viewed from the perspective of these cases or other Commission actions, there is no basis for suggesting that the Commission is insensitive to the specific concerns of the professions or that we are simply trying to impose unncessary regulation. To the contrary, if the Commission's antitrust authority in this area is taken away, the result will no doubt be less competition and more regulation. Quite frankly, at a time when marketplace principles are gaining ascendency, it would be a tragic shame for one of the most important sectors of the economy to be arbitrarily insulated from a major source of antitrust scrutiny.

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[2] Bates v. State Bar of Arizona, 433 U.S. 350 (1977); Virginia Pharmacy Board v. Virginia Consumer Council, 425 U.S. 748 (1976).

[3] *American Medical Ass'n* v. *Federal Trade Comm'n*, 638 F.2d 443 (2d Cir. 1980), aff'd by an equally divided Court, 50 U.S.L.W. 4313 (U.S. March 23, 1982).

[4] 15 U.S.C. §§44, 45(a)(2).

[5] It should also be emphasized that the Commission's position was supported in an amicus brief specifically rejected the argument that the Commission's order would encroach upon the power or authority of the states. To the contrary, the states argued that the Commission's action would enhance the authority of the states to deal with anticompetitive behavior by private professional associations. Brief for the States of Ohio, Arizona, Colorado, Connecticut, Iowa, Maryland, Minnesota, Nebraska, New Mexico, New York, North Carolina, Pennsylvania, Rhode Island, and West Virginia as Amici Curiae in Support of the Federal Trade Commission at p. 29.

CONSUMER UNFAIRNESS

In recent years, much of the controversy surrounding the Commission's activities has focused on the scope of the agency's authority to reach unfair acts or practices. In particular, the controversy has had far less to do with individual cases than it has with proposed rules, where unfairness issues have been more prevalent. Some rules based at least in part on an unfairness rationale are now in effect, such as the Commission's rules applicable to care labels for clothes, door-to-door sales and the rights of consumers when third party financing is involved (the so-called holder-in-due-course rule). Other rules have not yet received final Commission consideration.

Perhaps the most universal complaint about the agency's unfairness jurisdiction was that it lacked clear definition and could be susceptible to subjective interpretation. To meet these concerns, the Commission undertook a major effort in 1980 to articulate the principles that guide us in this area. That process culminated in December 1980 with the issuance of a Policy Statement. In that statement the Commission delineated two fundamental issues for determining whether a business practice is unfair: (1) whether the practice causes unjustified consumer injury, and (2) the extent to which other public policies, legislative or judicial, impact upon the practice. The latter criterion is largely a supplementary consideration that helps to facilitate the analysis of consumer injury. As the Commission noted in its 1980 Policy Statement, a thorough review of relevant public policies "can serve as an important check on the overall reasonableness of the Commission's actions."

As to the primary issue of consumer injury, the Commission had this to say:

"To justify a finding of unfairness the injury must satisfy three tests. It must be substantial; it must not be outweighed by any countervailing benefits to consumers or competition that the practice produces; and it must be an injury that consumers themselves could not reasonably have avoided."

Thus, the injury test is one of balancing direct consumer harm against any offsetting business justifications to ascertain the net effects of the practice on consumers. In many ways, this process is analogous to the rule-of-reason analysis applied to antitrust issues. In my view, the Commission's Policy Statement provides a rational framework for analyzing unfairness.

The more immediate question is whether Congress should go beyond the Commission's 1980 effort and attempt to write some more specific standards into the law. On this point, I share the Chairman's view that legislation would be helpful, not only as a means of providing guidance to business but also as a way of enhancing the Commission's authority. Unlike some of the other areas of the Commission's jurisdiction, such as deception, there is far less case precedent clearly defining the parameters of the consumer unfairness standard.

At the same time, while legislation can be of value, I strongly believe that it should reflect the criteria already set forth by the Commission in its 1980 Policy Statement. Those criteria, I believe, should satisfy any concerns that the Commission may rely on less than objective factors in addressing unfairness issues. Further, if Congress agrees with this approach, I would urge that the legislative history reflect the kind of analysis set forth in the 1980 Policy Statement.

Turning to the question of advertising and unfairness, I find myself in partial agreement with the advertisers. Deception should be the primary standard for judging advertising and the First Amendment severely limits the extent to which the Commission or other government agencies can regulate truthful advertising. Nevertheless, I do not believe that advertising should be exempted from the unfairness test. While there may be few instances where an unfairness test will be suitable for advertising, I can think of situations where an unfairness rationale may be more appropriate than deception. For example, consumers may act to their detriment in purchasing a product because of erroneous assumptions about the product's performance or side effects. If these erroneous assumptions are cause by the advertising, we have a classical deception case. However, advertising may not always be the direct cause of mistakenly held beliefs about a product; in such circumstances an unfairness approach may be appropriate to help assure that the advertising in question does not contribute to substantial consumer injury.

Another problem with removing advertising from the reach of unfairness is defining what constitutes advertising. In its broadest definition, it could literally encompass every verbal or spoken communication between sellers and buyers. If interpreted in such a fashion, the exemption could affect marketing activities that have little to do with traditional kinds of commercial advertising.

I do believe, however, that the Commission should exercise great restraint in pursuing advertising under our unfairness authority. That kind of approach makes sense from a policy perspective and is consistent with Constitutional protections afforded nondeceptive commercial speech.[6]

DECEPTION

The Chairman has suggested that Congress write into the law a definition of deception that would: (a) look to the reasonableness of consumer behavior; (b) require the deception to be material to the purchase decision; and (c) distinguish between representations of fact and opinion. Although I disagree on the approach, I fully share the Chairman's objective of reexamining Commission policy in this area to make sure that we avoid strained interpretations of ad claims and do not pursue trivial cases.

I believe the Commission has made good progress in its case selection process during the past few years. For example, we have attempted to focus our resources on cases where consumers cannot easily verify the attributes of a product either before purchase or through inexpensive repeat purchases. Additionally, we have looked at situations where there may be no readily understood common denominator for describing the attributes of a product. In such cases, self-interest may drive firms to describe their products in favorable terms that are not comparable to other similar products. The lack of a uniform standard of reference can facilitate a welter of confusing and misleading claims.

But no matter how carefully cases are selected, the process still involves a great degree of pragmatic judgment, especially with respect to the interpretation of advertising claims. Since it would not be feasible for the Commission to conduct a survey of consumer beliefs before bringing each case, we must, of necessity, frequently look to the ads themselves to determine what representations they convey. This direct form of examination, of course, may be supplemented through the testimony of marketing experts or by reference to any explanatory information in the hands of advertisers. The upshot is that a good dose of commonsense is required in the selection and prosecution of advertising deception cases.

That process does not mean the law is standardless, but it does suggest the need for careful articulation of the enforcement criteria employed by the Commission. Not only do advertisers rely on such decisions but many others do so as well, including state consumer protection agencies (which enforce "little FTC" statutes) and self-regulatory bodies, such as the Better Business Bureau's National Advertising Division. As the lead agency for interpreting the law of deception, it behooves the Commission to clarify current policy as clearly as possible and indicate the extent to which outmoded or ill-conceived principles are no longer in use.

One way to clear up any uncertainty and correct past mistakes is by amending the law. That approach helps to assure that policy changes become relatively permanent and are less subject to change depending upon the make up of the Commission. The other major approach is to have the Commission undertake a thorough review of past advertising cases and set forth in some detail which principles we still adhere to and which we don't. The virtue in this course is that guidance can be provided without changing the basic contours of the law.

For my part, I favor the latter approach because I believe the basic structure of deception law remains sound. Under current law, a challenged ad claim be a reasonable interpretation of an advertisement, the claim must be material to consumers and the kind of claims generally subject to challenge must be factual representations, not personal opinions or puffery. In my view, any shortcomings in enforcement policy rest not so much on the inadequacy of applicable legal standards as they do on the manner in which those standards have been applied to individual cases in the past.

To change the law at this time could lead to new uncertainties because any change, even if it generally tracks existing law, is likely to be read by the parties and the courts as a departure from past practice. That is especially true here since the law of advertising deception has been relatively well settled for a long time. It seems to me that changes in advertising deception policy can best be handled by the Commission in the first instance either in the form of policy guidelines or within the context of adjudicated cases. Moreover, although a legislative redefinition of deception will cabin the Commission's discretion to some extent, it will be necessary to leave considerable room for the Commission to determine, for example, what constitutes a reasonable interpretation of an advertising claim. Thus, a legislative approach carries with it the risk that the new law will remain unsettled for a period of time while, at the same time, it seems likely that the courts will continue to give great weight to the agency's interpretation of advertising claims as well as the materiality of those claims.

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[6] See Central Hudson Gas and Electric Corp. v. Public Service Comm'n, —— U.S. ——, 100 S. Ct. 2343 (1980).

Nevertheless, although I do not support legislation, I want to reiterate my support of the Chairman's efforts to review Commission advertising policy and to make whatever changes are called for.

National Council of Senior Citizens,
Washington, D.C. April 12, 1982.

Hon. Robert Kasten, Jr.,
Chairman, Subcommittee on Consumer Affairs, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

Dear Mr. Chairman: I am writing on behalf of the membership of the National Council of Senior Citizens to express our deep concern over proposals to restrict the Federal Trade Commission's authority over the professions. We believe that the FTC's activities regarding doctors, dentists, optometrists and other state regulated professional have served the interests of American consumers and that narrowing the Commission's authority in this area would be a serious mistake.

As you may know, we have consistently opposed efforts to grant professionals special status under the FTC Act or to limit in any way their obligation to comply with Federal antitrust and consumer protection laws. The FTC's efforts to increase competition and lower prices for professional services are of vital importance, particularly in times of spiraling inflation. Our members must have the information necessary to shop wisely for eyeglasses, hearing aids, dentures and health care services. The FTC has helped insure that this information is available. Our members must also be protected against physicians' attempts to boycott health insurers' cost containment programs and efforts by professional societies to fix prices. The FTC has actively fought such activities.

We have not received this type of protection from state regulation. We cannot look for protection to state regulatory boards dominated by the very profession they claim to regulate.

We followed with great interest the hearings on the FTC and the professions held in July 1981. We believe that the evidence produced at those hearings provides no sound justification for granting special treatment to the professions and that accordingly the FTC's authority over state regulated professions should be left intact.

The National Council of Senior Citizens, as you may know, is a membership organization composed of 4,000 state and local senior citizen clubs, representing more than 3.5 million older persons nationwide. Many of our members are dependent upon fixed incomes and are acutely affected by the FTC's efforts to promote competition among professionals. We hope that, as you formulate your position regarding FTC jurisdiction over the professions, you will give full consideration to the views that we have expressed.

Sincerely,

William R. Hutton, *Executive Director.*

American Dental Association,
Washington, D.C., April 15, 1982.

Hon. Robert W. Kasten, Jr.,
Chairman, Subcommittee on Consumer, Committee on Commerce, Science, and Transportation, Russell Senate Office Building, Washington, D.C.

Dear Mr. Chairman: The American Dental Association, on behalf of its more than 130,000 members, appreciates this opportunity to present its views to this Subcommittee in connection with hearings held with respect to the reauthorization of the Federal Trade Commission. The Association requests that this statement be made part of the record on these hearings.

As you are aware, in July 1981, the Association filed a statement and presented testimony before this Subcommittee outlining the dental profession's concerns with FTC activities which have exceeded their Congressionally mandated authority with respect to jurisdiction over non-profit professional associations and to abrogate state laws and regulations regarding the regulation of the delivery of dental care.

Inasmuch as the Association has so recently apprised this Subcommittee of these activities its reasons for resisting these unauthorized incursions by the FTC into oral health care delivery system, this statement will be restricted to the urgent need for legislation to clarify FTC jurisdiction and authority with regard to state regulated professions such as dentistry.

Notwithstanding the Subcommittee's oversight hearings on FTC activities concerning professionals in July, 1981 and the implementation of a major reorganization at the FTC, the Commission, to date, is continuing its investigations with regard to the dental profession, particularly with respect to lay ownership of dental practices and the provision of denture care by nondentists.

To date, the Commission has not informed either dental profession or to our knowledge, members of this Subcommittee, under what statutory authority it is conducting these investigations. Besides the absence of statutory authority, it is our opinion that FTC and its staff lack the needed expertise to evaluate the health care consequences and other potential problems for patients who require dental care services that would be unalterably and adversely affected by the override of state laws that presently maintain the high standards of quality of dental care rendered by dentists who have met extensive educational and licensing requirements.

In light of these continuing FTC activities, the recent Supreme Court split decision in the *American Medical Association* v. *Federal Trade Commission* only further underscores the need for Congress to clarify the FTC's jurisdiction and authority over state regulated professions, such as dentistry.

While this split decision affirms the ruling of the lower appeals court, it certainly did not represent a clear-cut mandate for the FTC. Apparently, at least four of the participating justices believed that the FTC did not have jurisdiction over professional associations.

Mr. Chairman, as you are aware, Senators James McClure and John Melcher along with four members fo the Commerce Committee have introduced S. 1984 which would clarify FTC jurisdiction and authority with regard to state regulated professions, such as dentistry, as well as establish some needed procedural reforms in the FTC Act.

The Association supports this legislation as a means to restrain many of these unauthorized activities that the FTC is continuing to engage in regarding the dental profession.

To a great extent, these FTC activities have not focused on violations of the antitrust law, but rather attempts to make social policy judgments and override state laws on who is qualified to render health care services to the public.

This proposed legislation would not grant immunity to the professions from enforcement of the antitrust laws at either the federal or state levels. Instead, it would curb these unauthorized and unnecessary regulatory intrusions by the FTC into policy areas that have been traditionally regulated at the state level.

In conclusion, we believe it is time for this Subcommittee and Congress to adopt statutory limits, such as those contained in S. 1984, on FTC jurisdiction and authority with respect to professions in order to clarify the present uncertainty in law and to restrain these unnecessary FTC activities and investigations.

Sincerely yours,

ROBERT H. GRIFFITHS, D.D.S.,
President.

THE STATE OF COLORADO,
DEPARTMENT OF LAW,
OFFICE OF THE ATTORNEY GENERAL,
Denver, Colo., April 20, 1982.

Senator ROBERT KASTEN, Jr.,
Senate Consumer Subcommittee,
Russell Building, Washington, D.C.

DEAR SENATOR KASTEN: I believe that the proposed amendments to section 5(a) of the Federal Trade Commission Act adding restrictive definitions of unfair or deceptive acts or practices would leave both federal and state consumer protection law in chaos. In Colorado, as elsewhere, state courts interpreting our consumer protection act have relied on federal judicial construction of section 5(a). See, e.g., *People ex rel. Dunbar* v. *Gym of America, Inc.*, 177 Colo. 97, 493 P. 2d 660 (1972). Changing the language of the Act at this late date would cast doubt upon the validity of this well-established federal and state precedent. Moreover, because of such reliance on federal case law, giving restrictive definitions to "unfairness" and "deception" at this point in time would severely hamper state courts' efforts to give the legislatively-intended effect to consumer protection statutes.

In addition, the restrictive language of the various proposals for amending section 5(a) would seriously jeopardize the effectiveness of the Commission by requiring it to meet a much greater burden of proof. This, in turn, would necessitate an even greater expenditure of the Commission's resources than occurs at present. Yet, only last week the Commission announced plans to close its Denver office and those in three other locations, with an attendant reduction in personnel. It is inconceivable that the Commission could continue to deal effectively with deceptive trade practices in these areas if, in the absence of such regional bases, it is nevertheless called upon to expend greater efforts to meet a higher standard of proof. Thus, it would be left to the states to take up the slack against deceptive trade practices by increasing enforcement activities under their consumer protection statutes. However, the states are in no position to do so. In addition to the precedential problem noted above, the states do not have the necessary resources to undertake such efforts. In Colorado, for example, due to budgetary cutbacks by the legislature my antitrust and consumer protection staff has been reduced by virtually half-from 7 attorneys and 4.5 investigators to 4 attorneys and 2.25 investigators—in just the past year.

In adddition to opposing any redefinition unfairness or deception in section 5(a), I also wish to express my strong opposition to efforts by the professions to have themselves exempted from coverage under the Act. As Chairman Miller has observed, the effect of such special interest legislation would be to artificially raise prices for services that are already frighteningly expensive. Thus, it would make quality professional services available to fewer people who need them.

I have advocated free competition in the marketplace since my tenure in the Colorado legislature, when I actively sought to insure that consumer protection legislation also treat businesses fairly. However, I believe the proposed legislation to limit section 5(a) and exempt the professions would vitiate two decades worth of federal and state efforts against practices that have caused both innocent consumers and honest businesses irreparable damage. Accordingly, I strongly urge that you vote against the proposed amendments to the Act.

Very truly yours.

J. D. MacFarlane, *Attorney General.*

Federal Trade Commission,
Washington, D.C., April 22, 1982.

Hon. Slade Gorton,
U.S. Senate,
Washington, D.C.

Dear Senator Gorton: Thank you for your letter of March 24 requesting my views on the 1982 FTC Reathorization. I appreciate the opportunity to comment and apologize for the delay in my response.

Given the number and nearly infinite variety of proposals urged on the Congress in connection with our reauthorization, I have an admittedly wide field to comment on. Perhaps it would be most useful for me to concentrate on those areas where I believe the proposals are the most damaging to the Commission's law enforcement efforts or most negative in terms of the public interest. Proposals in those categories include:

(1) The proposed exemption of the "professions" from FTC jurisdiction. The Commission unanimously opposes this proposal.

(2) The proposed amendment to Section 5 to give clearer meaning to "unfair" trade practices. I do not oppose amending the statute to include the principles enunciated in the Commission's December 1980 policy statement on unfairness jurisdiction. I do oppose the advertising trade associations' request to exempt commercial speech from "unfairness" coverage.

(3) Proposals (various) to redefine and narrow the Commission's authority to police deceptive trade practices. I am unalterably opposed to all of these proposals, as are Commissioners Clanton and Pertschuk and The National Association of Attorneys General.

(4) The proposal to eliminate FTC jurisdiction where it is complementary with any other fedeal agency or department. I oppose enactment of this proposal because it would result in a near total removal of the Commission's jurisdiction, which is no doubt its purpose.

(5) The proposal to repeal 5m(1)(B). I am opposed to repeal of this section of the Act which gives the Commission authority to seek civil penalties, upon proper notice, for violation of actions found illegal in prior cases.

I am enclosing several documents which provide an explanation of my views on these subjects. My testimony of April 1, 1982, to the House Subcommittee on Commerce, Transportation and Tourism of the Committee on Energy and Commerce, presents in some detail the reasons for my opposition to any exemption for the professions and to a new, restrictive statutory definition of "deceptive trade practices." A summary of my views on the latter is also contained in the enclosed copy of an article I authored for Advertising Age on April 12, 1982.

Because I understand that Tim Muris' memo recommending amendment to Section 5's deception standard is actually being favorably received by some Members of the Senate, or their staffs, I have prepared a brief critique of it, which is also enclosed. Basically, I do not have great objection to the standards he proposes, if they were proposed for use as prosecutorial guidelines—that is, for use as case selection criteria or even as guide-posts for ultimate decision-making. To amend the statute, however, is another matter altogether which will inevitably produce years of confusion and uncertainty for business and advertising agencies and for law enforcement at the federal and state levels.

In addition, the advertising trade associations have made an eleventh hour decision to "support Chairman Miller's" effort to redefine "deception." Their proposal, however, differs markedly from his and introduces a whole new set of problems which I have highlighted in the attachment.

I have also taken this opportunity to comment further on the proposed exemption of the professions from antitrust and consumer protection scrutiny and on the proposal to eliminate the FTC's complementary jurisdiction with other agencies.

Thank you for this opportunity to present my views. If I can provide any additional information or be of assistance to you in any way, please let me know.

Sincerely,

PATRICIA P. BAILEY, *Commissioner.*

Attachments.

COMMENTS ON 1982 FEDERAL TRADE COMMISSION, REAUTHORIZATION ISSUES, PATRICIA P. BAILEY, FTC COMMISSIONER

EXEMPTION FOR STATE-LICENSED PROFESSIONALS

Trade associations representing doctors, dentists, veterinarians and the like, have proposed that "professionals," i.e., persons with graduate degrees who are licensed by a state, be exempted from the nation's consumer protection laws and from antitrust scrutiny by the FTC. That proposal is apparently being taken seriously by the Congress. As a member of one of those "professions," I find that distinctly embarassing. Politically, it strikes me as a virtually unexplainable proposition. How is the voting public to understand or to accept that the possession of a "professional" license entitles one to immunity from laws the vast majority must continue to obey?

The FTC has long been active in scrutinizing professional activities from both antitrust and consumer protection perspectives. None of these efforts is directed at interference by the Commission with the state licensing of professionals. The education, training, testing and licensing of professionals to perform is not our concern. That is the business of each state. Our concern goes only to activities which violate the antitrust laws and to self-imposed professional restriction on the ways in which state licensed services can be delivered to the public.

The Commission's interest in looking at professional self-regulating restrictions is aimed at determining whether those restrictions, for whatever reasons they may have been adopted, restrain the practice of that profession in such a way that available services are restricted and prices inflated. Sometimes we find that even though the restrictions may have those undesirable effects, they are, on balance, justified by the need to maintain the quality of care delivered to the public. In that case, we back off. But, since doctors and dentists and others tend to assert that every restriction they adopt is designed solely to ensure the quality of care the profession delivers, it is not surprising that we have, on occasion, disagreed with them in concluding that easing those restrictions would lower prices, increase services and result in no loss of care quality. That was exactly the situation when the Commission promulgated the Eyeglasses Rule and witnessed significant consumer savings even in the first year it was in effect. Before the rule, by one means or another, opticians, or sellers of eyeglasses, were not allowed to advertise, allegedly because quality of care would suffer.

Because we knew that the price of glasses in states where advertising was permitted was between 25 to 40 per cent lower than in those where advertising was not permitted, the Commission undertook exhaustive research to be sure the claims about quality of care were groundless. Then we promulgated the Eyeglass Rule. Within one year, the price of eyeglasses in those states where the restrictions were lifted were clearly affected. While medical care costs in general were rising at the rate of about 10 per cent annually, eyeglasses increased in price at the rate of only about 5 per cent. There was absolutely no loss in the quality of care delivered.

When we discuss this program we most often talk of savings to consumers—and they can be substantial. But more is involved. The potential extension of available services is involved, and the greater utilization of trained professionals is involved. For example, in some places, obstetricians may have made it possible for nurse midwives to obtain hospital beds for their patients. On the average, from conception through delivery, an obstetrician spends a total of about 3½ hours with a patient and charges about $900. Nurse midwives spend an average total of about 26 hours with a patient during the same period, at an average cost of between $500 and $800. Many women, for financial or emotional reasons, prefer the services of a nurse midwife. Why can't those women, wherever they live, get admitted to a hospital for delivery or for emergency service?

There are many categories of health professionals, who are educated, trained and licensed by the states to perform certain medical services and who are able and willing to perform those services at lower costs for more people. What we are trying to discover, hopefully with the cooperation of the professions, is whether or not by easing some restrictions they might be able to practice more freely without endangering the quality of care delivered. This could be especially important to people who now have little or no access to any kind of regular, minimal care—like those in the inner cities and in many rural areas or in institutions.

Often these professionals—such as nurses, nurse midwives, nurse practitioners and dental hygenists to name a few—cannot offer their services as widely and at the lower prices they would charge because, among other reasons:

They cannot get hospital beds for their patients; they cannot work unless in the physical presence of a doctor, or dentist; their services are not reimbursed by medical insurance plans; or they cannot advertise.

It is in many ways a genuine tragedy. The fact is, there are legions of trained and licensed professionals who are restricted in their ability to deliver care; many of them now work only part time, if at all. At the same time, American paid $247 billion for health care last year, and medicare/medicaid payments are soaring to incredible levels. We cannot afford to ignore any circumstances which may cause the under utilization of available talent. I simply cannot believe, in these circumstances, that the Congress is being urged to remove all of these problems from the scrutiny of the only agency of the national government that is looking at them in an innovative and constuctive way.

THE COMMISSION'S DECEPTION AUTHORITY

In my House testimony and the article I wrote for Advertising Age, I explain at some length my misgivings concerning the Chamber/NAM and Chairman Miller's proposals to narrow the Commission's jurisdiction over deceptive trade practices. Commissioners Clanton, Pertschuk and I are joined in these concerns by the National Association of Attorneys General. The NAAG Executive Committee passed a unanimous resolution opposing these proposals at its meeting in Washington on March 26–28, 1982. (A copy of that resolution is attached.) In it resolution, NAAG noted that the proposed changes to the FTC Act "would circumscribe the scope of consumer protection statutes at the state level and would undermine the ability of the states to protect their citizens."

When I prepared hy House testimony, I had not yet received a memorandum dated March 25, 1982, from Timothy J. Muris, Director of the FTC's Bureau of Consumer Protection, which explains in some detail how the Chairman's proposed changes to the deception standards should operate in practice. I have since read Mr. Muris' memorandum and would like to take this opportunity to comment on it.

At the outset, I should make it clear that I support many of the principles Mr. Muris espouses; the difference between us is that I believe the Commission should adopt them internally as criteria for case selection and ultimately for decision-making but not as new statutory standards. Indeed, Mr. Muris has chosen my dissent in the *Kroger* matter as a example of the kind of reasoning he believes the Commission should embrace in future cases. Clearly, I too have been troubled on occasion by insufficient reliance on consumer survey evidence concerning the meaning of ads and by inordinately strained interpretations of allegedly deceptive claims that could fool only the most credulous.

Mr. Muris cites some examples of "bad" cases which would be prevented by the statutory changes he and the Chairman propose. While I might disagree with his condemnation of some of these cases, any catalogue of alleged "mistakes" the Commission may have made in the last 44 years is really beside the point. No statutory change can ensure that "bad" cases (assuming we could agree on a universal definition of "bad") will never be brought; only judicious Commissioners, exercising their collective discretion to the best of their ability, guided by Congressional oversight and the federal courts, can prevent mistakes. But what is most troubling about Mr. Muris' explanation of the new standards is the difficulties they would pose, if inserted in the statute, for the efficient prosecution of "good" cases.

For example, Mr. Muris writes in his memorandum, "[A reasonableness] standard, however, would not impose any significant barrier in those cases that the Commission should prosecute. It would not require surveys or other extrinsic evidence in all cases, indeed, such evidence would be necessary only in that small class of 'close' cases." (emphasis in original) (page 11) I find this purported explanation of the way his new statutory standards would be applied facile and hence disturbing. If his standards for case selection were used as internal guidelines by the Commission, then I believe he is correct. That is the way they should work and very likely most "mistakes" could be weeded out in close cases. But the state and federal courts do not assume that the Congress legislates for no purpose. If a standard as well developed in the case law as "deception" is altered, the courts will rightly assume that Congress intended to change the law. Most of our cases, "good" or "bad," are appealed to the federal courts, which have the last word. It seems distinctly unlikely to me that federal judges, faced with a new statute, will allow the Commission to instruct them about "good" and "bad" and to tell the court when (because the Commission says the case is good) the court should continue to follow previous law and allow inferences of consumer injury and harm, and when (because the case is close) the court should follow the new law and require survey evidence as to an ad's meaning and *proof* of actural injury and actural harm to consumers. It seems much more likely to me that the new statute would be read to require detailed consumer survey evidence documenting the Commission's interpretation of *all* allegedly deceptive advertising, however blatant or obviously false the Commission finds it to be. This kind of evidence will be expensive and burdensome to produce—and the advertisers will share that burden with the Commission. The predictable result is fewer cases and far more lengthy proceedings to resolve the few that are brought.

A similar problem arises in Mr. Muris' discussion of how the Commission would go about proving that deception caused "substantial consumer injury." He writes in his memorandum, "A requirement that the Commission in fact prove that this kind of injury is likely before it finds an ad deceptive is *not* a requirement for quantitative cost-benefit analysis in advertising cases. Nor need injury be measured in monetary terms. Rather, in most instances, a logical inference that injury is likely to exist would suffice, subject, of course, to rebuttal by the respondent's evidence." (Emphasis in original—page 22.)

Even assuming that the Commission could distinguish between cases where a "logical inference" of injury would be appropriate and those where it would not and that the courts would accept our distinction without question as within our discretion (which is doubtful), some extensive documentation of injury would almost always be necessary to meet the respondent's inevitable evidence that consumers were not materially harmed by the proven deception. Once again, I reiterate that I agree with Mr. Muris that the Commission should focus its limited resources on cases where deception can cause the greatest injury to consumers. But once we have proven a claim is false, or unsubstantiated, we should not also have to examine what the product was really worth to consumers or what opportunities for benefit they missed by buying it rather than some other product.

In an effort to explain how the proposal would screen out cases where no injury occurred, Mr. Muris cites the recycled oil cases where the Commission found that it was deceptive to sell recycled oil without disclosing that the oil was, in fact, recycled. Since there is no difference in performance between recycled oil and oil refined from virgin crude, Mr. Muris concludes that no injury occurred, despite the Commission's undisputed finding that consumers prefer the product made from virgin oil. Mr. Muris argues that had consumers realized the equivalence in performance of the two products, they would not have had an irrational preference for the virgin oil. I do not disagree with this conclusion, although Mr. Muris does not explain why sellers of recycled oil could not claim equivalent performance at the time they disclosed that their product was recycled. But I find the implications of his analysis troubling. Is the FTC to become an arbiter of consumer taste, judging what is good or bad for consumers in the guise of an economic analysis of consumer injury? Once again, the courts' inability or unwillingness to follow Mr. Muris' carefully constructed interpretive rules could lead to this result.

I would also point out that Mr. Muris' otherwise thorough memorandum does not discuss the ramifications of his proposal for the Commission's advertising substantiation program. Representatives of two advertising trade associations have informed me that they do not believe the proposal will affect the substantiation doctrine, which is based in large measure on the Commission's deception authority and forms the underpinning of the industry's own self-regulatory program. I believe they are wrong. In order to prove or even to infer injury, as a statutory requirement, the Commission would, it seems to me, have to prove that the claim was false—i.e. that the product lacked the attribute the advertiser of seller claimed for it. It seems quite unlikely that the Commission could show that a claim which was simply unsubstantiated (or made without a reasonable basis to believe it was true—as opposed to being plainly false) caused the kind of concrete, measurable injury that is contemplated by the proposal. Thus, the entire, substantiation doctrine would be called into question, if not shortly disregarded.

The existence of the Commission's ad substantiation program is clearly important to the advertising community. They know well the positive overall effect it has had on their industry and its image with the public. Yet the advertising trade asociations have just in last few days decided to join in the clamor for alteration of the deception standard (in addition to their earlier request to be exempted from the "unfair" standard.) Their proposed reformulation of the deception standard is different from that proposed by Chairman Miller and Mr. Muris. According to a press release issued on April 13, 1982, the Associations advocate the following statutory language:

"Deceptive acts or practices in or affecting commerce are declared unlawful where such acts or practices—

(1) consist of material representations known to be false or made in reckless disregard of their truth or falsity, or

(2) consist of misrepresentations that directly cause or may foreseeably result in substantial economic injury to consumers acting reasonably under the circumstances."

The press release clearly states that the associations intend any new definition to require "bona fide ad substantiation."

Association representatives have said to me that it is the first prong of this two-part test—statements made in reckless disregard of truth or falsity—that would be the standard governing substantiation cases. The second prong of the test, of course, is similar to Chairman Miller's proposal.

Although the advertisers believe that the substantiation program, and other cases challenging deceptive advertising, could continue under this "recklessness" standard, I doubt whether the Commission would pursue a credible law enforcement program should it be enacted into law. "Recklessness" is an extremely high legal standard, never before a part of the law governing advertising. To apply it in this area, the courts will turn to the case law libel and torts, from which the standard is directly derived.

In the well-known cases of *New York Co.* v. *Sullivan,* 376 U.S. 254 (1964) and *Time, Inc.* v. *Hill,* 385 U.S. 374 (1966), the Supreme Court articulated the standard for libel concerning matters of "public interest" as "proof that the defendant published the report with knowledge of its falsity or in reckless disregard of the truth." The Supreme Court has consistently emphasized that such a high standard for libel in cases involving public officials or matters of public interest is necessary in order to safeguard First Amendment guarantees of free speech and a free press. It is probably unnecessary to point out what is generally conceded: given the "reckless" disregard standard and the virtual impossibility of proving it, public officials and public figures cannot hope to win a libel case except perhaps in the grossest kind of circumstances.

Commercial speech, on the other hand, was not held by the courts to be entitled to basic First Amendment protections until the mid-1970's. The Supreme Court's most recent explorations of the constitutional protections to which commercial speech is entitled is *Central Hudson Gas & Electric Corp.* v. *Public Service Commission of New York,* 447 U.S. 557 (1980), where the Court held that a three-part balancing test should be applied in deciding whether an infringement on commercial speech is constitutional: (1) the speech must concern lawful activity and not be misleading; (2) it must be determined whether the asserted governmental interest to be served by the restriction on commercial speech is substantial; and (3) if both inquiries yield positive answers, it must then be decided whether the restriction directly advances the governmental interest asserted and whether it is the least drastic alternative available.

Thus, it is clear that the recklessness standard for libel concerning matters of public interest and the *Central Hudson* three-part test stand at opposite ends of the spectrum of constitutional protections afforded these very different types of speech. The advertisers ask the Congress to cut the FTC's ability to police deceptive advertising back to the libel standard. Such a change would mean that consumers would have no more protection from deceptive advertising than public figures have from free-wheeling (and often false and damaging) press commentary about them.

The second place to look for the legal meaning of "recklessness" is tort law. The term "recklessness" is applied there to actions of gross negligence and has been described as one of "quasi-intent". In the state of Washington, for example, the courts have held that a person who drove at 50–60 miles per hour without slowing down between a row of parked cars and a truck, all of which were standing with their headlights on and so close together so that there was barely enough room to pass, and struck a pedestrian, was behaving recklessly. *Liebhart* v. *Calahan,* 434 P. 2d 605 (Wash. 1967). It is difficult to imagine what kind of dramatically irresponsible conduct an advertiser would have to engage in before its actions reached an analogous level of recklessness. I think we can predict some decidedly bizarre results should the courts ever have occasion to apply the tort standard in an FTC advertising case.

Of course, the strategy here may be to have the advertisers so far out on a limb that Mr. Muris' proposals sound moderate and reasonable. And of course they are, if applied internally as guidelines. Both proposals are radical, however, from the point of view of the disruption they will cause to state and federal law enforcement in an area which is now well established and well understood.

Finally I would point out that all of those proposals and the discussion about them ignores the highly significant point that "deceptive trade practices" is a far wider category than just advertising. Neither the Chairman nor the ad associations (though they more understandably) have concerned themselves in these proposals with their potential impact on the myriad of deceptive practices challenged by the Commission and the states over the years which have nothing to do with advertising. For that reason alone the Congress should hesitate to alter this statutory standard pending at least a review of the impact of a new statute outside the world of Madison Avenue.

FTC COMPLEMENTARY JURISDICTION

The chamber of Commerce has proposed that the Congress prohibit the Commission from reaching conduct "that is authorized by federal statute or subject to the direct regulatory authority of another federal agency." (See Senate Commerce Committee Testimony, March 19, 1982, at pages 30–33.)

The apparent rationale behind the chamber's proposal is that it is inappropriate for the Commission to assume the role of an "all purpose" consumer protection agency when Congress already has established numerous other regulatory bodies to provide protection in specifie areas or has acted to exempt certain parties or conduct from federal regulation. However, it is the Commission's belief that the addition of such sweeping language to Section 5 is both unnecessary and ill-advised for several reasons.

First, the Congress has a number of more direct methods currently available to it, such as the use of specific exempting language or exclusionary provisions in an agency's authorizing statutes, to address issues of overlapping jurisdiction.

Second, viewed strictly in terms of its substantive merits, the Chamber's proposal would effectively prohibit the FTC from using its Section 5 authority in areas where both Congress and the courts have already made clear that the FTC shares authority over a number of practices, such as those involving advertising, credit and land sales, with other federal agencies. In fact, despite the existence of complementary jurisdiction in certain areas, the courts have determined that the FTC is often the agency with *primary* enforcement authority and expertise in the regulation of unfair and deceptive practices. See, e.g., *FTC* v. *Sperry Hutchinson Co.,* 405 U.S. 233 (1972).

Third, the examples cited by the Chamber in its accompanying statement to the Senate Committee on Commerce, Science and Transportation as evidence of the Commission's misue of overlapping jurisdiction are entirely inapposite. The Chamber cites the Commission's use of Section 5 to reach parties or conduct specifically exempted by Congress from requlation under the Fair Debt Collection Practices Act (FDCPA). In fact, it was largely as a result of the Commission's exercise of its Section 5 authority in the debt collection area that prompted the Congress to enact the

FDCPA in the first instance, and the legislative history to the Act reveals clear Congressional intent that the Commission continue to police the activities of creditors and others not covered by the Act.

Finally, the Chamber's proposed amendment poses procedural problems for the Commission of an undetermined but potentially unlimited magnitude. Because of the myriad of federal statutes that may overlap with the FTC Act in some fashion, even read narrowly the amendment protends a confusing, cumbersome and costly review process to determine under what circumstances the Commission may proceed with any individual enforcement proceeding. Read more broadly, the proposed language could effectively exclude the Commission from a wide array of rulemaking and adjudicatory endeavors undertaken by the Commission both currently and in the past. While the list of potentially prohibited undertakings is too exhaustive to include here, examples of areas in which the Commission might will be forced to defer to other agencies include food and drug advertising substantiation matters; FDCPA related cases; Truth-in-Lending Act cases which also involve potential Section 5 violations; fraudulent land sales cases; and auto and other product defects cases.

TESTIMONY OF COMMISSIONER PATRICIA P. BAILEY

Mr. Chairman and members of the Committee, it is a pleasure to be here today, with my collagues, to discuss the Federal Trade Commission's 1982 reauthorization. This process just two years ago resulted in several fundamental reforms to the agency's operations. I know that you have invited us here today to offer what assistance we can in explaining the possible ramifications of a series of additional proposals advanced, mainly, to deal with the business community's continued perception that the Commission needs checks on its statutory authority to prohibit unfair and deceptive practices in the marketplace. It will be obvious to you, as we do so, that there are some areas where we disagree on how best to address the persistent criticisms leveled at our agency. To a great extent, these disagreements are the healthy byproduct of a collegial body like the Commission, which has a long tradition of intense internal debate about the agency's mission.

These disagreements, however, should not divert attention from the large areas of consensus among us. We are, for example, unified in our opposition to perhaps the most important special interest proposal pending before you: The removal of the professions from antitrust and consumer protection scrutiny.

Also, we are unified in a belief that, should the Congress feel it necessary to define with greater specificity the Commission's authority to police unfair trade practices, it should do so by adopting the standards the Commission articulated in its December 1980 statement on that subject. Finally, although we have varying views on the precise level of funding appropriate for the agency, we all recognize prevailing national policies of budgetary restraint and we are committed to assisting Chairman Miller in his efforts to streamline and manage as efficiently as possible the daily law enforcement activities of the agency.

In my statement today, I will focus on the three central substantive proposals to amend the FTC Act which have been presented to the Committee: first, the total exemption of state-licensed professionals; second, the exemption of commercial advertising from the Commission's jurisdiction over unfair trade practices; and, finally, the adoption of a more narrow definition of the Commission's jurisdiction over deceptive acts or practices. I will, of course, by pleased to answer any questions the Committee may have.

JURISDICTION OVER THE PROFESSIONS

The law enforcement initiatives and economic studies which have provoked pleas that you exempt the professions from the Commission's jurisdiction are referred to generically within the agency as the "occupational *de*regulation" program. I emphasize the "de" in "deregulation" because I think that one syllable most accurately summarizes the overriding goal of all our efforts in this area. And, Mr. Chairman and members of the Committee, let me assure you that I recognize the difference between *de*regulation and regulation. I have, as you know, appeared before you on two occasions to defend the Commission's efforts to regulate, if only mildly, used car sales, and I am carefully attentive to the difference between regulation and deregulation.

As the Commission has repeatedly pointed out, most recently in our letter to Senators Packwood and Kasten last month, the occupational deregulation program combines traditional antitrust enforcement with efforts to challenge restrictions on advertising and other forms of commercial practice by competing health professionals.

Thus, we have brought cases involving allegations of price fixing, boycotts and other private agreements or conspiracies to restrain or eliminate competition by other health professionals.[1] Other rules and enforcement actions have been patterned on landmark Supreme Court cases such as *Virginia State Bd. of Pharmacy* v. *Virginia Citizens Consumer Council*[2] and *Bates* v. *State Bar of Arizona*[3] which recognized that competitors and consumers may have a constitutional right to the free flow of truthful commercial information. The Commission's theory in these initiatives is that unwarranted restrictions on commercial speech are also unfair to competitors and consumers.[4]

One major objection to the occupational deregulation program which has been advanced by some professional groups is that it interferes with the states' right and responsibility to supervise the quality of health care received by their citizens. There are two basic responses to that concern. First, the Commission draws a sharp distinction between regulations designed primarily to ensure quality of care and those that merely restrict business practices which, if permitted, could enhance competition. Our deregulatory efforts are focused on the latter type of restriction. Of course, in any area as complex as health care regulation, quality of care issues can become interwined with what appear to be purely commercial considerations. In those instances, the Commission demands a rigorous showing that any efforts on our part to enhance competition in the commercial aspects of health professionals' practice will not undermine efforts to ensure the quality of care given to the public.

Second, I believe that the Commission has shown and will continue to show extreme sensitivity to the concerns and prerogatives of the states. We have studied carefully the federal courts' development of the state action doctrine, which has established standards for federal government scrutiny of practices which are not directly regulated by the states. As a matter of policy, the Commission has clearly adopted this doctrine as an integral part of case selection criteria. I am firmly committed to a continuation of that policy.

Recognition of clear state prerogatives in this area, however, does not mean that we cannot contribute significantly to continued efforts to deregulate the health care marketplace. Put simply, we can offer the perspective of 67 years of antitrust and economic expertise on a national scale. Our contribution may be unique and I can only hope that we will be able to continue to explore ways in which to address any legitimate problems that may arise due to any overlaps between our jurisdiction and that of the states. The Commission has moved very cautiously in this area and no actions which we have taken in the occupational deregulation program in any way justifies the total exemption of any professional group or groups from antitrust and consumer protection jurisdiction.

Before I leave this subject, let me offer one final thought. When we talk about the benefits derived from the occupational deregulation program, we think primarily in terms of consumer dollars saved. Another clear and related benefit of efforts to deregulate the marketplace is the potential for increased services to those who have little or inadequate access to any of them now. There are many classes of professionals who strive for the chance to offer different forms of health care services to the public. Dental hygienists, nurse practitioners and nurse midwives—to name just a few—all have a tremendous stake in the success of these deregulatory efforts. Those trained in these professional categories view their work, not as a substitute for, but rather as a complement to the kind of health care offered by the dominant sectors of the medical profession. One has only to look at the state of health care services available in the inner cities and in many rural areas of the country to understand the compelling need to expand the availability of their services.

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[1] See, for example, *American Medical Association*, 94 F.T.C. 701, 996 (1979), *aff'd* 638 F. 2d 443 (2d Cir. 1980), aff'd per curiam, No. 80-1690 (Slip op. March 23, 1982). See, also, consent agreements involving *Indiuna Dental Association*, 93 F.T.C. 392 (1979); *Forbes Health Systems Medical Staff*, 94 F.T.C. 1042 (1979); *American Society of Anesthesiologists*, 93 F.T.C. 101 (1979); and *Hope, et al.*, Docket No. 9144.

[2] 425 U.S. 748 (1976).

[3] 433 U.S. 350 (1977).

[4] See, for example, the Eyeglasses Rule, 16 CFR 456, which was upheld in part and remanded in part by the D.C. Circuit in *American Optometric Association* v. *FTC*, 627 F.2d 896 (D.C. Cir. 1980).

UNFAIRNESS AND COMMERCIAL ADVERTISING

As I mentioned at the beginning of my statement, the Commission is united in its recommendation concerning the standards Congress should adopt should it determine that a more specific definition of the Commission's authority to proscribe unfair trade practices is necessary. Those standards, taken from our December 1980 policy statement, include (1) whether the practice causes substantial injury to consumers; (2) whether such injury is reasonably avoidable by consumers; and (3) whether the injury is outweighed by any countervailing benefits to consumers or competition derived from the practice. The Commission should also consider whether the practice violates any established public policy.

The only point I would highlight concerns the type of analysis the Commission should be required to undertake in evaluating offsetting benefits and costs. As we noted in our letter to Senators Packwood and Kasten, there is a risk that a benefit/cost analysis requirement could unnecessarily complicate or delay an investigation or litigation if the requirement is read to mandate a highly quantitative, dollar and cents kind of result. In many cases, a far more subjective analysis would be the more reasonable approach. This observation is especially important in cases where we have adopted a remedy which gives business many future options. For example, we might impose an information disclosure requirement that could lead a company either to negotiate over price, to offer increased warranty coverage or to adopt a satisfaction guaranteed or dispute resolution program. In such cases, we may have difficulty predicting with precision the dollars and cents benefits which will be achieved by consumers. Any requirement that we quantify such benefits before the remedy has had a chance to take effect will only serve to limit our flexibility in adopting the most reasonable alternative approaches to the problem because it will force us to select a single, rigidly defined remedy with easily predictable results.

Despite what I consider to be the Commission's strenuous efforts to articulate the standards we have used in exercising unfairness authority (the months of meetings leading up to the December 1980 statement are still clear in my mind), the advertising community, has urged the total exemption from the FTC's unfairness jurisdiction for "commercial speech". As much as I regret the fundamental difficulties which occurred in recent years between the Commission and some segments of the advertising community, I cannot endorse on any basis this kind of extreme approach to perceived problems which can be, as recent history illustrates very well, addressed in other forums and dealt with effectively. The plain fact is that if the advertisers prevail with their proposal, those ultimately injured will be not only consumers but members of the advertising industry. I think it extremely likely that the public will perceive the exemption they seek as a license to perpetuate unfair advertising in the media. However simplistic and, arguably, unfair this perception may be from the industry's perspective, I believe it will occur and that it could undemine decades of cooperative work to build the public confidence in the integrity of advertising which has come to exist.

Finally, I would bring one disturbing and possibly unintended ramification of the proposal to the committee's attention. As explained in their testimony before our Senate oversight committee last month, the advertisers propose that "the Federal Trade Commission Act be permanently amended to provide that the term 'unfair . . . acts or practices' does not apply to commercial speech." (emphasis added)[5] Read both literally and broadly, this proposal could exempt virtually any form of interchange between seller and consumer including promotional materials distributed at the point of sale, sales presentations to groups of potential buyers or even one-on-one conversations between a sales representative and a consumer. Thus, even the most blatant forms of high pressured sales solicitations could be exempt from challenge.

As a companion to their proposal that commercial speech be exempted from the FTC's jurisdiction over unfair practices, the advertisers also ask that you repeal Section 5(m)(1)(B). That section gives the Commission the authority to go to federal court for civil penalties if a company violates prior adjudicated determinations of the Commission with "actual knowledge" that the conduct had been previously declared unlawful. The advertisers argue that unless Congress repeals this authority, the Commission could use previous unfairness cases to seek civil penalties against many members of their industry, thereby accomplishing "back door" rulemaking concerning unfairness.

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[5] Joint Statement of the American Advertising Federation, the American Association of Advertising Agencies and the Association of National Advertisers Proposing and Supporting Amendments to the Federal Trade Commission Act (at page 6) before Subcommittee on the Consumer, of the Committee on Cmmerce, Science and Transportation of the United States Senate (March 19, 1982).

In considering this proposal, it is important to understand exactly how Section 5(m)(1)(B) operates. The typical case begins with the Commission serving a synopsis describing the conduct previously determined to be unlawful on industry members who may be engaging in similar practices. The synopsis is accompanied by a letter warning the recipient that the Commission may seek civil penalties if the conduct does not cease. All recipients, as a matter of policy, are given a period of time to bring their practices into compliance. If the alleged violations persist, the Commission may consider filing a complaint in federal district court. However, the Commission has always conceded, and one district court has held, that during the subsequent court proceedings the recipient of the synopsis must have an opportunity to argue not only that it did not engage in the conduct alleged to be unlawful but also that the Commission's prior determinations concerning the illegality of such conduct were wrong.[6]

The Commission's authority under Section 5(m)(1)(B) has proven to be an extremely effective and efficient way to enforce the law. Perhaps the best recent example of its use involved 67 companies, primarily sellers of new homes, which received letters and synopses in 1979 concerning the deceptive advertising of interest rates. Given the volatile state of the housing market, accurate interest rate information has become perhaps the most important single factor affecting consumers' search for a home. The Commission became concerned about possible deceptive advertising in this area after receiving several complaints from homebuilders alleging that their competitors were advertising artificially delfated rates in an effort to attract customers who would not discover the true rate until the transaction was well advanced.

After giving the 67 companies several months to come into compliance with the law, and offering to advise them informally concerning their compliance obligations, the Commission was able to close its investigations of 55 companies, or over 85 percent of those who receive synopses. We signed consent agreements with the remaining 12 companies, securing a total of $488,000 in penalties, all of which were subsequently approved by the federal district court. Apart from the high level of voluntary compliance achieved quickly and at a low cost through this program, I think it is noteworthy that the problem was identified in the first place by competitors' complaints about unlawful business practices. Repeal of Section 5(m)(1)(B) would inhibit the Commission's ability to protect not only consumers, but also honest business from unfair or deceptive trade practices.

REDEFINITION OF DECEPTION

Three different proposals to define by statute the Federal Trade Commission's jurisdiction over deceptive trade practices have been advanced in recent weeks. The first, contained in S. 1984, which was introduced by Senators McClure and Melcher, and the second, suggested by the Chamber of Commerce and the National Association of Manufacturers, would require application of cost/benefit analyses to cases challenging deceptive practices. The third, suggested by Chairman Miller, would (1) require a finding that the challenged act or practice was "material" as that term is understood in the common law; (2) exempt statements of opinion; and (3) limit deception to situations where "reasonable" consumers are likely to be deceived, except in cases where vulnerable groups of consumers are involved and the company knew or should have known a practice was deceptive.

I cannot agree that the Commission's deception authority should be redefined. I am unaware of any sustained criticism of the Commission's use of its deception jurisdiction by the business community. Those who must live with the standards of conduct the agency has developed over the years appear to understand pretty clearly both the law's parameters and the agency's procedures in enforcing it. But beyond the observation that the system seems to be working for all concerned, I believe considerable legal mischief would ensue should any change be made, no matter its purpose or intent. Prevention of deceptive practices would inevitably be made more difficult, time-consuming and costly at a time when shrinking budgets demand just the opposite result.

To understand the potential impact of each of the three proposals to redefine deception, it is necessary to analyze critically what such changes would mean to 44 years of precedent defining the agency's and the states' authority to proscribe deceptive practices and therefore how the proposals would affect future federal and state enforcement in this area.

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[6] *U.S.* v. *Braswell, Inc.*, No. C81-558A (N.D. Ga, 1981), reported at *CCH Trade Cases* ¶64,325 (1981).

I emphasize state enforcement because one important aspect of any revision to Section 5 which is all too often overlooked is the impact it would have on state law enforcement. Any changes to Section 5 of the Federal Trade Commission Act would also change the law in many states which have adopted "little FTC Acts" modeled on the Federal law. Forty-nine states and the District of Columbia have enacted statutes more or less like the FTC's to prevent deceptive and unfair trade practices. In many of the states, these "little FTC Acts" track the FTC Act's exact language, and several states either by statute or court decision also provide that Commission cases shall be used in interpreting the scope of state law.[7] It is clear, then, that the states would be bound by any limitation of the FTC's authority to police deceptive practices, and to the degree that confusion and uncertainty over the scope of our jurisdiction followed such a change, the same confusion and uncertainty would also be introduced into state enforcement activities. I have attached to this testimony a recent resolution adopted unanimously by the Executive Committee of the National Association of Attorneys General which opposes proposed amendments to Section 5's prohibition on unfair or deceptive acts or practices because of their potential impact on state law.

The above noted, as I believe it must be, I do not see the need for any change in Section 5's deception standard.

The FTC Act has prohibited "deceptive acts or practices" since 1938, and during the intervening 44 years there have been hundreds of administrative and judicial decisions construing that term. Even before the 1938 Wheeler Lea Amendments added jurisdiction over deceptive practices to the FTC Act, a large body of common law had developed the concept of false, deceptive or misleading trade practices. Since 1938, cases brought under the UCC and other states laws have continued to amplify on these concepts and on the principle that fraud in the inducement of a contract, through misleading representations or material omissions of fact, is illegal.

A large body of case law has developed in this way, and there is little evidence that I am aware of that the authority to prohibit deceptive practices has been used by the FTC, (or the states or private litigants for that matter) in a manner that has consistently injured consumers or business—except, of course, for those businesses that have engaged in deceptive practices. Without some substantial indication of what types of worthwhile business practices are supposedly being stifled by the application of the current statutory definition, Congress is being asked to remedy a "problem" which cannot be demonstrated to exist.

It is no trivial matter to alter 44 years of jurisprudence. If the prohibition on "deceptive practices" is altered, no matter how benign the intentions of those making the change, the natural assumption of the legal community, including state and federal judges, will be that Congress intended to change the actual effect of the law. The inevitable result will be that at least some deceptive practices which are now illegal under current law will become legal, as judges and lawyers are cast adrift from precedent to search for the new law's meaning. Only one thing is certain—any change will be a bonanza for lawyers. With 44 years of legal doctrine tossed out the window, every new FTC case will have to be decided without the benefit of established precedent.

The first step then for lawyers representing a company that has been sued by the FTC for engaging in "deceptive practices", no matter how blatant the clients's practices, would be to ask the agency or the federal courts to reconsider the action, and determine first whether the lawsuit could be justified under the new statutory standard. Added litigation and delay in the work of the Commission and the courts is virtually certain. Further, any change could cast into doubt the validity of hundreds of cease and desist orders issued in accordance with past precedent. It is fully predictable that the agency would be flooded with requests to reopen and reconsider all orders issued over the past four decades. This kind of administrative nightmare could also occur on the state level, particularly in states which pattern enforcement on FTC precedent.

Let me turn now to an analysis of the possible ramifications of the proposals which have been advanced thus far. The bill introduced by Senators McClure and Melcher, S. 1984, would require a showing that a deceptive act or practice "causes substantial consumer injury that outweighs the benefits derived from such act." The Chamber of Commerce and NAM have proposed to amend Section 5 to prohibit ". . . deceptive acts or practices . . . where such acts or practices directly cause or may foreseeably result in subtantial injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition . . .".[8]

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[7] See, e.g., statutes in *Illinois*, Ill. Ann. Stats. ch. 121-1/2 § 262 (Smith-Hurd 1960 & Supp. 1981); *Washington*, Wash. Rev. Code Ann. § 19.86.020, .920 (1978 & Supp. 1981); *Massachusetts*, Mass. Gen. Laws Ann. Ch. 93A § 2 (West 1972 & Supp. 1981); *Maryland*, Md. Com. Law Code Ann. §§ 13-105, 13-301, 13-303 (1975 & Supp. 1981); *Maine, Me.* Rev. Stat. Ann. title 5 § 207 (1979 & Supp. 1981); and *New York*, N.Y. Gen. Bus. Law § 349 (McKinney Supp. 1981).

These proposals appear similar in intent—i.e. to apply a requirement that the Commission find costs outweigh benefits before prohibiting deception under Section 5. However, since the Chamber and NAM have discussed in some detail how they intend such a provision to operate, I will focus my comments on their proposals. I would note, though, that the kind of approach taken in S. 1984 could easily pose the same problems for future Section 5 enforcement that I identify below.

The Chamber of Commerce and NAM have charged that in applying its authority to proscribe deceptive acts or practices, the Commission has ignored the "requirement" intended by the Congress that it prove consumers suffered "actual injury" as a result of the deceptive practice. The Chamber and NAM explain that proof of "actual injury" means proof that consumers would have made a different purchasing decision but for the deceptive misrepresentation. They have criticized a long line of Commission cases, upheld by several federal circuit courts, which stand for the principle that the Commission need not probe the minds of all those who heard the deceptive statement to determine whether they would have bought the product without it; rather, the Commission need only show that the statement has the "tendency and capacity to deceive" consumers. Their proposal appears to be clearly designed to reverse this doctrine and to require instead that the Commission prove a direct causal link between the deceptive representation and substantial, "actual" consumer injury.

The Chamber asserts that its proposal would not impair the Commission's ability to condemn and prevent "actual" deception. It says that falsehoods and "intentionally misleading" representations have no proper place in a well-functioning free market and that "by their very nature" such "fraudulent" behavior is "intended to inflict and does inflict substantial injury on consumers." Because such conduct "has no redeeming virtue and cannot reasonably be avoided," Commission enforcement actions against such acts or practices could continue under the Chamber/NAM proposal.[9]

Despite the Chamber's contention that law enforcement efforts against "actual" deception could continue uninterrupted, it is clear that both the Chamber and NAM intend their proposal to change dramatically the burden of proof the Commission must assume to prove even a false (much less a misleading, or unsubstantiated) advertising case:

"[The proposal] would require the Commission to take questionable consumer practice one step beyond the intuitive finding that conduct may potentially or even actually result in consumer injury. The *Commission would be required to show, on the record, that the actual injury at issue could reasonably have been foreseen.* Thus, the Commission must clearly prove that enough information exists by which the Commission can draw the conclusion that absent federal intervention injury is not only likely to occur, but is foreseeable under the circumstances." (emphasis added)[10]

Perhaps the most helpful way to illustrate how the Chamber/NAM proposal could operate in practice is to review how it would change the prosecution of one of the

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[8] The Commission itself, in December 1980, formulated the "substantial injury/not reasonably avoidable/not outweighed by countervailing benefits" standards in explaining the exercise of its authority to proscribe *unfair* trade practices. These standards were derived from an analysis of all prior unfairness cases. That analysis took several months and involved a painstaking effort both to describe the development of unfairness doctrine and distinguish it from the development of deception doctrine. Any effort to apply the unfairness standards to the Commission's deception authority ignores the separate development of these two doctrines and would be done without the benefit of a responsible analysis of how the deception doctrine has evolved over 44 years in both federal and state caselaw. (See Letter from Federal Trade Commissioners to Senators Wendell H. Ford and John C. Danforth (December 17, 1980). See also the Commission's opinion in the matter of *Horizon Corporation,* Docket No. 9017, Slip op. at 62 (May 15, 1981), which incorporated the standards stated in the letter.)

[9] Statement of the Chamber of Commerce (at page 28) before the Subcommittee on the Consumer of the Commerce, Science and Transportation Committee, United States Senate (March 19, 1982).

[10] *Statement of James F. Carty on Behalf of the National Association of Manufacturers* (at page 9) before the Subcommittee on the Consumer of the Committee on Commerce, Science, and Transportation, United States Senate (March 18, 1982).

Commission's best-known false advertising cases—the case involving Listerine mouthwash.[11]

That case challenged the claim that Listerine could "cure" or "prevent" colds, which was one of several claims included in a typical advertisement for the product. The Commission proved to the satisfaction of the circuit court of appeals that there probably is no "cure" for the common cold and that, in any event, Listerine certainly was not such a cure. Satisfied by this fundamental finding of false advertising, the court upheld the Commission's order barring future misrepresentations and requiring corrective advertising to reverse the general misimpression in the minds the American public that gargling with Listerine every morning would prevent colds and sore throats.

Under the Chamber/NAM proposal, future Listerine cases could not be considered in nearly such a straightforward manner. In fact, as I read the proposal, the Commission could be forced to jump through the following procedural hoops in order to find the same violation of Section 5:

First, we would have to conduct a statistically valid survey to prove that a substantial number of the consumers who bought the mouthwash after seeing the ad did so because they thought it would cure colds and not for any other reason. It would not be enough for us to draw the common sense inference that this central claim probably caused consumers to purchase the product; instead, we would have to prove a direct causal link between the claim and their behavior.

Second, once we had proven that a substantial number of people bought the product only because they thought it would cure colds, we would then have to explore whether consumers could have avoided any injury caused by their purchase of the product. Could they, and if so, how long would it take for them to discover that repeated applications of the mouthwash did not dispose of their colds?

Once we had assembled empirical evidence to show that consumers could not discover Listerine's failings for themselves—by proving through expert testimony, for example, that all colds go away sooner or later anyway and so it is hard to tell whether time or mouthwash "cures" them—we would then have to explore exactly what kind of injury consumers suffered when they bought the product. Did they pay more for Listerine? Even if they did, could the Listerine have helped ease their cold symptoms more than other products and was the additional relief worth the extra money? What was the alternative to Listerine? Another, cheaper mouthwash which was not as good? Or no mouthwash at all? What are the health or cosmetic benefits of using a mouthwash? What if consumers hadn't bought Listerine or any other mouthwash but instead had realized they needed to buy a completely different kind of symptom reliever? Would those other products have been effective? Answers to all these questions could be necessary to demonstrate and quantify the "actual" injury caused by the concededly false advertisement.

Finally, under the Chamber/NAM proposal we would have to show that this injury "reasonably foreseeable" by Listerine. In the original case, the company had some inadequate studies showing that Listerine might help ease the symptoms of a cold. Would these studies immunize its false advertising from an FTC "cease and desist" order? Why should intent be an element of proof when the remedy for the practive is not criminal but merely a prospective order prohibiting its repetition?

The preparation of the kind of case I have outlined above would be very costly not only for the Commission but also for the respondent company. The higher the FTC's burden of proof, the more information we would have to obtain by compulsory process from the target of an investigation. We would undoubtedly bring far fewer cases, but the targets of those we did bring might soon wish the definition of deception had never been changed.

In addition to severely complicating the prosecution of a straight falsity case, the revised standards of proof could also have the effect of eliminating the Commission's advertising substantiation program because it might be almost impossible for us to establish a casual link between the lack of substantiation and consumer behavior. The purpose of the ad substantiation program is to encourage advertisers to have support for the claims they make before disseminating commercial messages. Under the Chamber/NAM proposal, we might have to prove that had consumers known a specific claim could not be substantiated, they would have changed their purchasing behavior. We might also have to prove that the claim was in fact false since otherwise it would probably be argued that consumers suffered no injury from relying on it.

In sum, the Chamber of Commerce and NAM proposal could require the Commission and the states to carry a well-nigh impossible burden of proof by having to demonstrate that the majority of those exposed to a deceptive claim would have made a different purchasing decision but for the deception.[12] The proposal would appear to threaten the Commission's advertising substantiation program, which is the basis for an extensive network of industry self-regulatory mechanisms. At the same time, it would cast doubt on 44 years of precedent and cripple the Commission's efforts to exercise its authority to proscribe deceptive acts or practices for many years to come.

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[11] *Warner-Lambert Company* v. *FTC*, 562 F.2d 749 (D.C. Cir., 1977).

Chairman Miller has proposed to redefine deception by incorporating a "materiality" element, exempting statements of opinion and limiting the agency's jurisdiction to practices which would deceive only "reasonable" consumers, except in those cases involving practices aimed at vulnerable groups where the Commission could show the company "knew or should have known" the practice was deceptive.

It is my understanding that a "material" misrepresentation, under the common law, is a misrepresentation on which consumers are likely to rely in making a marketplace decision. The Commission and the federal courts have already construed Section 5 to apply only to "material" misrepresentations.[13] However, the Courts have recognized that the Commission may reasonably infer that a deceptive statement would materially affect consumers' marketplace decisions without requiring the Commission to conduct an expensive survey of actual consumer behavior. If addition of an express "materiality" standard to the FTC Act would mean imposing this type of proof requirement before the Commission can prohibit a demonstrably deceptive statement, the Commission will find it prohibitively expensive to pursue many cases of false advertising in the marketplace for the same reasons noted in my comments on the Chamber/NAM proposal. If the Chairman's change is not designed to eliminate the Commission's authority to infer materiality, then the change is unnecessary. Unfortunately, however, courts do not assume that Congress legislates without effect, and so any change is likely to invite litigants and judges to read in the proof requirement noted above.

As for the second, change, limiting deception to statements of 'fact," not "opinion," I would observe that existing law already makes that distinction to the extent it is desirable, and the proposed modification is likely at best to sow confusion and at worst to provide a refuge for future false advertising.

Courts have long recognized that "mere puffery" is not actionable by the FTC. If a claim is not objectively verifiable, and is by its nature a matter of opinion, an advertiser cannot be sued for making it. For example, the statment "our cookies taste best" is clearly puffery. On the other hand, the statement "you can earn $100,000 a year as our franchisee" is a statement that can be verified by experience and supported by analysis, and an advertiser will be held liable for its accuracy and supportability.

Explicitly limiting the ban or "deception" to statements of "fact" invites unscrupulous advertisers to dress up misleading statements in the guise of opinion, in order to take advantage of the express exemption granted opinion statements.[14]

The third proposed change would inject a requirement that consumers behave "reasonably" before they are entitled to protection by the FTC. For vulnerable groups like children or the elderly, who presumbly are not capable of behaving "reasonably", the Commission would have to show that a company "knew or should have known" the practive was deceptive.

As the law now stands it protects against any claims likely to deceive a substantial number of citizens. No inquiry is required to determine whether the conduct of those fooled meets some undefined standard of "reasonableness." In practice, of course, the Commission would not pursue a case involving conduct that would be likely only to fool someone behaving capriciously. The difficulty with the proposed change is that it could be read as a direct repudiation of the existing judicial standard, which was designed to protect the average consumer from deception.

Take, for example, the following quotation from a 1942 case involving the sale of a product called "Triple X Compound", which had been advertised as a cure for delayed menstruation in women. The product was both ineffective and dangerous. The advertiser argued that its artfully worded advertisements did not literally claim the product would be effective and that consumers (especially reasonable ones, presumably) should have understood the literal meaning of the ad. In rejecting this argument, the seventh circuit Court of Appeals wrote:

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[12] In the case of advertising in the mass media, the Commission would presumably have to track down not only all those who saw the ad, but also those who subsequently brought the product.

[13] *FTC* v. *Colgate-Palmolive*, 380 U.S. 374, 392 (1965).

[14] If the Chairman's standard is meant to turn on "substance" rather than "form" (i.e. whether consumers actually understand a statement of opinion as a statement of fact, regardless of whether the word "opinion" is used), then the standard will add nothing to existing law except confusion and litigation as lawyers and judges struggle to determine just what change the new provision is intended to effect. For an example of existing law that already draws this distinction, see *Kochk* v. *FTC*, 206 F. 2d 311 (6th Cir., 1953).

"The law is not made for experts but to protect the public—that vast multitude which includes the ignorant, the unthinking, and the credulous, who, in making purchases, do not stop to analyze but too often are governed by appearances and general impressions . . . . Advertisements are intended not "to be carefully dissected with a dictionary at hand, but rather to produce and impression upon prospective purchasers." *Aronberg* v. *FTC*, 132 F.2d 165, 167 (7th Cir. 1942).

Would this case be overruled by a reasonableness requirement? Perhaps that is not the intent of the proposal but it is by no means certain what kinds of consumer behavior could be labeled "unreasonable" by the courts. To cite just a couple of examples; is it "reasonable" to buy undeveloped land sight unseen? Tens of thousands of consumers have done so and, where the Commission found the sales pitch they were given was deceptive, we have obtained redress for them. Is it reasonable to permit yourself to be baited and switched to a more expensive product than you came to the store to buy? You are always free to leave the store and I can easily envision a court holding that "reasonable" consumers would have avoided being deceived by this practice which is routinely held to be deceptive.

As for the suggestion that the Commission prove that a company "knew or should have known" a practice affecting "vulnerable" groups was deceptive, I believe that an intent standard is certainly reasonable in a law that imposes monetary fines on an individual, and that standard already applies in the FTC Act where penalties are permitted.[15] But the FTC Act is also remedial. It is designed to protect consumers from false advertising and other deceptive practices, not to punish business. The only relevant question in determining whether to challenge a practice should be whether the practice is deceptive, not whether the person engaged in it knows it is.

If a company is engaged in a campaign of false advertising, and this can be proven, it should not also be necessary for the government to show that the company should have known its advertising was false before the false ads can be halted. A businessperson's intent does not mitigate injury to customers and competitors caused by false advertising. Further, the knowledge standard could be read to mean that a businessperson could only know that his or her practices were deceptive if they had been challenged in some other context before. Thus, the change could have the effect of introducing an actual notice requirement into the law, thereby virtually freezing the development of consumer protection at the date of its enactment. Ironically, the adoption of this standard would make it more, rather than less difficult for the Commission to protect vulnerable groups.

In closing, I would note that in developing his proposal, the Chairman has identified several past Commission cases which he believes were serious mistakes and which he believes could not be brought under a weakened test for deception. In one of the cases the Chairman cites (*Kroger*, Docket No. 9012), I dissented from the majority's finding of liability and discussed at some length why I thought the Commission's interpretation of the advertisement as deceptive was misguided. And while that is true and remains my opinion of that case, I do not believe that that dissent, nor any of the other cases cited by the Chairman, supports a modification of the deception standard for several reasons:

First, it makes no sense to me to jeopardize the results of hundreds of good and sensible cases in order to preclude a handful of ill-chosen ones about which business men and women have no serious concern. Second, the proponents of a weakened deception standard have given absolutely no indication at all of just how their various new standards would operate to eliminate the ill-chosen cases and at the same time enable the pursuit of meritorious cases without making prosecution of such "good" cases excessively burdensome, time-consuming and expensive. For example, if the new standard would operate to prevent one of the allegedly ill-chosen cases by requiring the Commission to produce a survey to prove that consumers relied on a false claim, instead of being able to infer reliance as it now does, then it is fully predictable that courts will similarly read the new standard to require a survey in a strong, meritorious case. While the Commission would theoretically be able to obtain such a survey in a strong case, it has not sought to do so in many cases involving blatantly false claims—including some brought by unanimous consent of the Commission within the past five months—both because such evidence is not required under current law and because of the substantial time and expense involved.

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[15] See 15 U.S.C. § 45(m)(1)(B).

Undoubtedly the Commission has on occasion brought ill-advised cases, just as other prosecutorial bodies have. But the solution for that problem lies in the exercise of better prosecutorial discretion, not in weakening the law in a way that threatens to make the large majority of justifiable cases much more expensive and difficult to bring. A law should be changed where there is a serious abuse that can be remedied, and the costs do not outweigh the benefits. In this instance, the proponents of a change in the deception standard have not pointed to any serious abuse, nor do I believe they have thought through the consequences of their proposals on the vast majority of the agency's cases. This is in part, no doubt, because those consequences are, in all honesty, impossible to predict.

I do not believe that most honest businessmen and women have any interest in weakening the laws that prevent deceptive commercial practices. The proposed change, while accomplishing no significant benefit, will enormously complicate, lengthen, and make more expensive the task of FTC attorneys who must endeavor on dwindling resources to prevent deceptive practices. Especially at a time when we have pledged to deliver to the public more value for less money, I must take strong issue with a legislative proposal that will almost certainly effect the opposite result.

[Advertising Age, Apr. 12, 1982]

WHY BAILEY OPPOSES "DECEPTION" RULE CHANGE

(FTC Chairman James C. Miller III quotes commissioner Patricia Bailey's dissent in the Kroger case to support his proposal for a tighter definition of the commission's authority over deceptive advertising. In this signed article, responding to an article by chairman Miller in Advertising Age March 22, commissioner Bailey warns that the proposed changes will legalize much that is considered deceptive now and will cause uncertainty for years to come.)

(By Patricia Bailey, Commissioner, Federal Trade Commission)

The new chairman of the *Federal Trade Commission,* the Chamber of Commerce and the National Assn. of Manufacturers have proposed to narrow the FTC's authority to challenge deceptive commercial practices. These proposals represent the first serious effort in 44 years to alter the FTC Act's prohibition against deceptive trade practices.

I oppose changing the deception standard, as do my fellow commissioners. A appreciate Advertising Age's invitation to express my point of view.

The Chamber/NAM proposal would require a rigid monetary cost/benefit analysis and would define deception by inserting in the Act the standards the commission now uses to evaluate a practice challenged as "unfair." Whatever the arguable justification for the first, the second would hopelessly confuse two distinct legal standards.

Chairman Miller's proposals appear to be aimed solely at advertising. And he has made them in the absense of any serious concern expressed by the advertising industry about the way the commission and the courts interpret "deceptive." In fact, I believe it is a fairly well understood standard. Indeed, it is a good understanding of what that law requires which forms the underpinnings of the industry's self-regulation mechanisms.

When a statute is changed, courts rightly assume a congressional purpose to change the law. I am convinced about the resulting confusion and uncertainty that will be introduced into the FTC's law enforcement efforts. I should think the advertising community would share that concern, and recognize the likely impact on its self-regulation scheme—as well as on the creative and legal departments of ad agencies across the country.

Chairman Miller's rewrite of the FTC Act would require the commission to prove "actual damage" to consumers before an ad could be considered deceptive. We would have to show that a substantial number of consumers saw an ad and then actually made a purchasing decision because of it. The courts now allow an inference that a substantial (although deceptive) advertising campaign influenced consumer behavior. Presumably we would have to prove that injury by using audience surveys showing that consumers relied exclusively on allegedly deceptive claims when buying the product.

Chairman Miller also proposes that the statute require that consumers only be entitled to protection if they behaved "reasonably." It is unclear exactly what "reasonable" behavior is in this context. The basic flaw in these proposals is chairman Miller's assertion that where "most" claims are concerned, it would be "obvious" that reasonable consumers would be deceived and suffer actual injury (obvious to whom?). He says that it would be only in those marginal cases where the commission's interpretation is "strained" that extrinsic evidence of "reasonable" and "actual injury" would be required I do not disagree that that should be the case. I just know that the courts would not have made any distinction based on what the FTC claims is "obvious" or "strained." They will, as they should, apply new statutory standards to all cases.

Chairman Miller would also exempt statements of "opinion" from coverage under the FTC Act. That would mean that virtually any "fact" claim preceded by the words "We think. . ." could be removed to an exempt category. Further, the chairman has said that "experts" should be allowed to express their views on any subject without interference. Thus, any false or misleading advertising claim could be immunized by placing it in the mouth of a willing "expert" endorser.

Some of the "ill-advised" cases the chairman has cited in his list of horribles date back to the early 1940s and '50s. That would be the period just following the original enactment of the deception statute. Many of those cases are the inevitable result of the enactment of a new statue. I predict a similar period of confusion and odd results should that now fairly well-defined standard be tampered with.

I know the chairman does not intend that result, and I do not doubt his intentions. The fact is, however, that no chairman or group of commissioners could control the federal courts' evaluation of the impact of new statutory standards. He is concerned that five unelected presidential appointees now make collective discretionary decisions. His proposal would remove this discretion from them and place it in the hands of *ad hoc*, any *one* of several hundred unelected presidentially appointed judges. No matter the sincerity and experience of those individuals, the result could be chaotic interpretation of the law for years to come.

I know there is tension between the FTC and some segments of the advertising industry. I know all about the proposed trade review regulation on children's advertising. There are undoubtedly those who are tempted to endorse any proposal to limit the commission's enforcement authority. But before leaping on that bandwagon, I think advertisers should ask themselves how they would feel if these potentially restrictive and confusing proposals were applied to the competitor complaints filed before the National Advertising Division of the Council of Better Business Bureaus and the National Advertising Review Board, let alone the FTC. Harm to consumers is not the only problem here. Harm to competition and to law-abiding competitors is also a serious concern. What would be the impact on the industry's self-regulatory program if all legal precedent and established standards were called into question?

If the FTC Act were changed of course, the NARB could choose to ignore the commission's new efforts to find a clear definition of deception. Advertisers would then have at least three standards to follow—those imposed by the FTC, the NARB and the states.

Advertisers and their agencies should also consider the likely experience of a target of the commission's investigation under these standards. To determine whether the ad is deceptive, that is, whether it deceived "reasonable" consumers and caused "actual injury," the FTC would have to conduct an exhaustive inquiry into virtually all aspects of a product's development and marketing campaign. There might be fewer cases, but those few would be extremely burdensome for the advertisers and agencies in—

I firmly believe that these proposals of chairman Miller and the Chamber/NAM are way of their intended target. They will not automatically ensure that a Federal Trade Commission will not bring some ill-advised cases. Only commissioners, exercising good judgment and using a sound set of policy criteria can do that. As a practical matter, I agree with many of the goals of the chairman's proposal. He cites my dissent in Kroger as the kind of reasoning the wishes to see the commission adopt. Obviously, I agree with that I am convinced, however, their changing the statutory standard will do nothing to ensure that result. What it will do is inject doubt into 44 years of jurisprudence and create uncertainty and confusion in commission enforcement and industry self-regulation as well.

Comptroller General of the United States,
Washington D.C., April 26, 1982.

Hon. Bob Packwood,
Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate.

Dear Mr. Chairman: Section 21 of the Federal Trade Commission Improvements Act of 1980 (15 U.S.C. 57a-1) provides for congressional review of final rules promulgated by the Federal Trade Commission (FTC). This section also requires that, before the end of fiscal year 1982, the Comptroller General submit a report to the Congress which:

(1) Lists the final rules submitted to the Congress by FTC.

(2) Lists the final rules disapproved by the Congress.

(3) Specifies the number of instances in which FTC promulgates a final rule after the Congress has disapproved the rule as originally submitted.

(4) Analyzes any impact that the congressional review requirement has had on FTC decisionmaking and rulemaking processes.

Pursuant to this requirement, we plan to issue our report to the Congress in September 1982. However, the congressional review provision and FTC's authorization for appropriations expire on September 30, 1982, and the Congress is now considering FTC reauthorizing legislation. This interim report discusses some issues that you may wish to consider to reduce delays caused by the congresssional review if this provision is retained.

This interim report is based on our examination of the rulemaking proceedings and other FTC records for the two rules submitted to the Congress for review. We also obtained the views of FTC Commissioners and staff, congressional staff, and others concerning the congressional review provision. Our review did not address the constitutionality of the congressional review process. However, we recognize that this issue is in litigation and may remain unresolved during the period in which the Congress is considering reauthorizing legislation for FTC. Our work was conducted in accordance with GAO's current "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions."

Section 21 of the act requires that FTC submit all final rules to each House of the Congress for review. If both Houses do not adopt a concurrent resolution disapproving a final rule within "90 calendar days of continuous session," it becomes effective on the date promulgated by FTC. Continuity of session is broken by an adjournment sine die (i.e., final adjournment of a session of the Congress). Also, the time during which either House is not in session for more than 5 days is excluded in computing the 90-day period. If the Congress adjourns sine die before the end of the 90-day period and before completing action to disapprove a rule, FTC must resubmit the rule to the next session of the Congress, and another 90-day review period begins.

FTC has submitted only two rules for congressional review—the games-of-chance rule and the used car rule. The game-of-chance rule, submitted on August 26, 1980, consisted of amendments to an existing rule. The amendments were deregulatory in nature, (1) lessening the recordkeeping and reporting burdens of participating retailers in promotional games of chance and (2) reducing the waiting period between games to 30 days or the length of the previous game, whichever is less. No resolution to disapprove these amendments was introduced before the 96th Congress adjourned on December 16, 1980. However, because 90 days of continuous session had not elapsed before adjournment, FTC resubmitted the amendments on January 27, 1981, for another 90-day review period, as required by section 21. Again, no resolutions of disapproval were introduced, and the congressional review period expired on June 1, 1981, about 9 months after the initial submittal to the Congress. The amendments became effective on August 17, 1981.

FTC submitted the used car rule for congressional review on September 9, 1981, during the first session of the 97th Congress. This rule would require car dealers to post a window sticker on each used car offered for sale disclosing to potential buyers whether any warranty was being provided and the terms of that warranty, listing any known major defects in the car's mechanical system, and disclosing certain other information. Resolutions were introduced in both Houses to disapprove the rule, and hearings were held to discuss its merits. However, a resolution of disapproval was not passed before the first session ended on December 16, 1981, after 86 days of continuous session from the date FTC submitted the rule for review.

Since the 90-day review period was not completed, FTC resubmitted the rule on January 28, 1982, during the second session of the same Congress, for another 90-day review period. New disapproval resolutions have been introduced, and further hearings have been held on the rule. If both Houses do not adopt a concurrent resolution disapproving the rule, we estimate that the 90-day review period will end on May 24, 1982, after the Congress will have considered the resolution for a total of 176 days (86 days during the first session and 90 days during the second). Thus, the congressional review will add about 9 months—from September 1981 through May 1982—to the rulemaking process.

We did not evaluate whether the 90-day review period gives the Congress sufficient time to consider FTC rules. However, FTC commissioners and staff, congressional staff, and other interested persons expressed the view that the current review period is too long.

MATTERS FOR CONSIDERATION BY THE CONGRESS

The experience with these two rules suggests that some features of the congressional review mechanism may unnecessarily delay the effective date of FTC rules. The congressional review process delayed the implementation of the deregulatory games-of-chance initiative (the only rule to complete the congressional review process to date) by about 9 months even though the rule was not controversial and no resolutions of disapproval were introduced. To avoid unnecessarily delaying the effective date of rules to which there is no congressional opposition, the Congress may wish to consider revising section 21 to provide that the review period will terminate after a short period of time (to be specified by the Congress) if a concurrent resolution of disapproval is not introduced.

Although the used car rule has not completed the congressional review process, this rule may remain available for consideration by the same Congress for as long as 176 days. To expedite the rulemaking process, the Congress may wish to consider revising section 21 to provide that, if the first session of a Congress adjourns before disapproving a rule within the original review period, the second session of that Congress shall resume consideration of the rule within the original period. During the second session, the review would continue for the balance of the period, or for some additional specified period.

To reduce delays caused by the 90-day review period, the Congress may wish to consider other options. For example, one option is changing the review period from 90 days of continuous session to 90 calendar days. Another option is changing the period to 60 calendar days, which is used in many other congressional review provisions. Both FTC rules discussed above had to be resubmitted—adding time to the rulemaking process—because of the current 90-day review provision. Had either of the above two options been in effect, the review period would have ended for both of these rules without the need for resubmission, thus reducing rulemaking time.

We hope that the information in this letter will aid your deliberations on the FTC reauthorizing legislation. Because the report contains matters for congressional consideration and does not make any recommendations or state any conclusions concerning FTC's activities, we did not obtain agency comments.

We are also sending this report today to the Chairman of the House Committee on Energy and Commerce; Senator Howard W. Cannon; and Congressman James T. Broyhill. We are sending copies of this report to the Chairmen of the Subcommittee on Consumer of the Senate Committee on Commerce, Science and Transportation and the Subcommittee on Commerce, Transportation and Tourism of the House Committee on Energy and Commerce. Copies are also being sent to the Director, Office of Management and Budget, and the Chairman of the Federal Trade Commission.

Sincerely yours,

Charles A. Bowsher,
Comptroller General of the United States.

Duke University
Durham, N.C., April 26, 1982.

Senator Bob Packwood,
Senate Office Building
Washington, D.C.

Dear Senator Packwood: I am writing to express my views on the pending proposal (S. 1984) to remove the licensed professions from the jurisdiction of the Federal Trade Commission. My interest arises from courses that I teach in the fields of antitrust law and health law and policy, including a seminar entitled "Antitrust and the Professions," at the Duke University School of Law. I have writtten extensively on antitrust and competition issues affecting the health care sector and published in March a book entitled Deregulating the Health Care Industry. In 1978–79, I served as a resident consultant with the FTC's Bureau of Competition and had an opportunity to see the Commission's work in the health care field at first hand. On the basis of this background and experience, it is my firm opinion that the FTC's activities affecting the health professions have been constructive and in the public interest.

Most of the FTC's efforts with regard to the licensed professions have occurred in health-related fields, and it is here that the impact of the proposed exemption would be greatest. Because the Commission has been the leading promoter of competition in the health services industry, termination of its role at this juncture and in this way would be most unfortunate. For one thing, it would seriously set back the progress that is being made toward making competition a reliable influence on industry performance and a force for cost containment. Moreover, to grant the health professions a gratuitous special exemption from FTC oversight at this time would signify that Congress, in addition to being reluctant to regulate the industry's overall economic performance, lacks a firm commitment to competition. In short, giving the professions a special status under the FTC Act would raise once again old doubts about whether the naiton has a coherent health policy.

In seeking this exemption, the dominant health professions are asking for much more than relief from overregulation or consumerist excesses. They are asking Congress to send a signal that the professions are to be spared both the full rigor of the antitrust laws, which insist on competition, and competition itself. If Congress should thus waffle on its commitment to competition, the effects would be felt, to consumers' disadvantage, throughout the health care industry. Without a clear national commitemt to competition and privately initiated change, private actors with an interest in cost control will continue to look to government for solutions to the cost problem. Even though some private actors—employers, unions, insurers, and independent providers—are beginning to recognize that they, rather than government, hold the best keys to cost containment, they need encouragement before they will challenge the dominant professional interests over the sensitive issues of price and utilization of services. For Congress now to penalize the single federal agency that has stood up against professional power would convey precisely the wrong message to everyone concerned.

I. THE FTC DESERVES PRAISE, NOT REBUKE, FOR AGGRESSIVELY ENFORCING THE ANTITRUST LAWS AGAINST THE DOMINANT HEALTH PROFESSIONS

Beginning under the Republican leadership of Chairman Engman and continuing under all subsequent chairmen, the FTC has pursued extensive inquiries into the reasons for the noncompetitiveness of the health services industry. Discovering a neglected agenda for antitrust enforcement, the Commission embarked on a campaign against a series of trade restraints systematically imposed by professional groups. The main focus of this campaign has been on ensuring that competition-stimulating cost-containment initiatives in the private sector are not suppressed by providers' unlawful action. I have followed the Commission's work in this field rather closely and find it to have been uniformly conscientious, procompetitive, and in the public interest.

Among the Commission's specific antitrust targets have been explicit professional boycotts aimed at health maintenance organizations, insurers, and others who sought to introduce organizational innovations and cost-control programs objectionable to professional groups. Professional efforts to discourage "contract practice" by declaring it unethical have been curbed, thereby facilitating wider use by third parties of provider "participation agreements" and the development of competing closed-panel mechanisms. The Commission's staff has also targeted direct control by dominant professional organizations of such financing mechanisms as Blue Shield plans and individual practice associations as another source of restraint on free competition among providers. Profession-sponsored restraints on professional advertising were also attacked in proceedings that yielded evidence of how professional groups harass individual professionals who take competitive initiatives threatening to non-competitive traditions and established market positions. Finally, moves by organized professional groups to preempt and foreclose independent decision making on such crucial economic issues as the level of fees and utilization have also come under scrutiny by the FTC staff. The net effect of bringing the antitrust laws to bear on these professional activities has been to open up new opportunities for fundamental change in health care financing and delivery.

The current movement to rebuke the FTC for its efforts with respect to the health professions is particularly ironic in view of the widespread agreement among informed scholars that these efforts have been in the public interest. In a recent article generally critical of the FTC's performance of its antitrust responsibilities, Professor Ernest Gellhorn of the University of Virginia Law School singles out the Commission's recent efforts with respect to the professions as virtually the *only* work of the Commission in the antitrust field that has been beneficial to consumers. (*Regulation*, Nov.-Dec. 1981, p. 32.) When even such skeptics as Professor Gellhorn and Chairman Miller himself approve of the Commission's work in the health care field, for Congress to curb the jurisdiction that has made this work possible would raise grave questions concerning Congress's commitment to the public interest.

II. THE FTC'S JURISDICTION OVER PROFESSIONAL AND OTHER TRADE ASSOCIATIONS SHOULD, IF ANYTHING, BE RECONFIRMED AND MADE EASIER TO ESTABLISH

The professional groups supporting S. 1984 claim that Congress must act to clarify the FTC's jurisdiction over professional organizations. Under current law, the Commission must establish its jurisdiction over nonprofit entities by showing that they are operated "for the profit of their members." In my view, this legal requirement is clear enough that no clarification is needed. I also believe, however, that it would be constructive to eliminate the requirement that combinations of competitors must be shown to have economic as well as other objectives before they are subject to FTC oversight.

A. *The Supreme Court's recent nondecision in AMA v. FTC creates no new uncertainties requiring legislative resolution*

The Supreme Court recently affirmed, by virtue of a deadlocked 4–4 vote, the decision of the U.S. Court of Appeals for the Second Circuit upholding an FTC order issued against the American Medical Association to terminate unlawful restrictions on professional advertising and "contract practice." American Medical Ass'n v. FTC, 50 U.S. Law Week 4313 (Mar. 23, 1982). Although one of the issues argued in that case was the construction of the FTC's statutory jurisdictional limits, there is no basis for concluding that the four justices voting to overturn the Commission's order did so on the basis of this jurisdictional issue. My own impression, which is confirmed by the opinion of the judge dissenting in the court of appeals, is that the other main issue in the case—whether the AMA had changed its conduct enough to obviate the FTC order—was much more likely to divide the Court. Thus, it would be a mistake to conclude, as the AMA is now arguing, that this case necessitates a congressional clarification of the Commission's jurisdiction over professional associations.

B. *If legislation is deemed necessary, it should eliminate the burdensome, Unnecessary, and polarizing requirement that the Commission establish trade and profession Associations' economic purposes*

The jurisdictional requirement of economic motives is gratuitous and complicates litigation unnecessarily. Because no FTC Act violation can be found in the absence of a probable adverse impact on competition or consumers, the law already protects against FTC interference with trade and professional association activities whose economic effect is not destruction. Furthermore, economic motivation is not an essential element in an offense against section 1 of the Sherman Act. Thus, the requirement that the FTC impugn the motives of professional organization as a predicate for antitrust jurisdiction raises a new and irrelevant issue, one that greatly increases litigation costs and generates more antagonism than would result from litigation on the merits. Finally, whatever reasons Congress may have had for limiting the FTC's jurisdiction over such nonprofit entities as universities and charitable organizations (I doubt that the limitation was a wise one), those reasons are unlikely to justify immunizing trade associations and other combinations of competitors.

The special jurisdictional requirement has the anomalous effect of making a competitor group's purity of motive a defense to an FTC proceeding when it would not be a defense in any other kind of antitrust action. This result is truly perverse. Many of the individual professionals engaged in collective action harmful to competition probably act for disinterested reasons, and their actions violate the law only because, proceeding from a purely monopolistic conception of the profession, they interfere with the development of competition. Because these professionals are involved in restraining trade only because they are acting with the tradition that their profession is to be viewed, managed, and reformed as a discrete economic entity, they should probably be exposed as little as possible to punitive antitrust sanactions. Thus, an action by the FTC, whose remedies have only prospective effect and carry a lesser risk of treble damages than actions brought by the Justice Department, would seem the best method for introducing professionals to their hitherto neglected responsibilities under the antitrust laws. For this reason, it would seem to make a great deal more sense to ease the FTC's burden in establishing jurisdiction than to foreclose that jurisdiction. That the professions themselves are seeking total relief from FTC scrutiny suggests that they are hoping for a signal from Congress that will bring about a relaxation of both the vigor of antitrusted enforcement against the professions and the applicable legal standards.

III. THE FTC'S POWER, UNDER CONGRESSIONAL OVERSIGHT, TO PREEMPT STATE LAWS IMPAIRING DESIRABLE COMPETITION IN THE PROFESSIONS SHOULD BE CLARIFIED, NOT CURTAILED

An assumption underlying the proposed FTC Act exemption for state-regulated professions is that state regulation satisfactorily safeguards both the consumer's interest as a purchaser of professional services and the federal government's interest as a major purchaser of health care. If, before accepting this premise, Congress were to hold extensive hearings to determine its validity, it would be discovered that state legislatures have often been manipulated by professional groups to enhance their market power. Indeed, the field of occupational licensure is notorious for the ways in which state legislatures have allowed themselves to be used to further private interests at the expense of competition and the consuming public. For example, a recent study of state regulation of the optometry profession has shown that the ability of professional optometrists to have their preferences served by state legislatures is a function of fortuitous political factors and that the consumer's interest is systematically neglected. Begun & Feldman, A Social and Economic Analysis of Professional Regulation in Optometry (National Center for Health Services Research, DHHS Pub. No. (PHS) 81-3295, 1981). Thus, there is no basis whatsoever for the suggestion that the existence of state regulation justifies granting the professions immunity from FTC oversight. Far from being a solution to the professions' noncompetitiveness and ability to exploit consumers, state regulation is frequently a major source of the problem. The federal policy of encouraging competition in the health care industry could easily be undercut by ill-conceived state regulation.

Although the federal government has a legitimate interest in checking the misuse of state power to suppress desirable competition among professionals, the appropriate extent of the FTC's power to preempt anticompetitive state laws is an important question. In a federal system, it may be unseemly for a federal agency to sit in judgment on state legislation. On the other hand, not only is there no denying that state law and regulation have frequently prevented desirable competition in the sale of professional services, but the FTC's work in this area of consumer protection has so far been circumspect and careful and very much in the public interest. The initiative to facilitate eyeglass advertising, for example, has been demonstrated to be in the public interest (see *id.*), although emerging constitutional doctrine may have eliminated the need for Commission action in that area. Other abuses by the states are less amenable to judicial remedies, however, and may be appropriate objects of the FTC's direct attention, with preemptive rulemaking a possible outcome. Although this should be a remedy of last resort, congressional oversight, through the mechanism of the legislative veto or otherwise, minimizes the danger that Commission rules will significantly infringe upon state sovereignty. It is likely that the FTC's main role will be as an expert advocate and publicist and as an independent source of ideas and data. Already, the publicity that the Commission has given to issues in the area of occupational licensure and regulation has contributed greatly to a reexamination of licensure laws and to increased awareness of the possible anticonsumer consequences of such regulation. Much more needs to be done, of course, on this front if the federal policy of promoting useful competition in the health services is not to be frustrated by anticompetitive action in the states.

A sensible resolution of the conflict between federalism concerns and the need for some federal check on anticompetitive state regulation has been achieved by the Supreme Court in what is sometimes called the "state-action" doctrine. E.G., *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. 97 (1980). It is probable that this doctrine confines the FTC's power just as it curbs the power of federal courts to invoke federal antitrust policy to invalidate a well articulated state policy decision to substitute a responsible regulatory regime for competition. There has been no judicial ruling on this question, however. Because of the serious federalism issue presented, it would probably be desirable for Congress to clarify that the FTC's power to preempt state law and regulation is subject to the state-action doctrine. Well conceived state legislation would thus be beyond the FTC's reach, but specific abuses would remain remediable under congressional oversight.

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Thank you for considering my views on this important question. Please let me know if I can be of further assistance.

Very truly yours,

CLARK C. HAVIGHURST,
Professor of Law.

STATE OF LOUISIANA,
DEPARTMENT OF JUSTICE,
Baton Rouge, La., April 27, 1982.

Hon. ROBERT PACKWOOD,
Chairman, Senate Commerce Committee,
Washington, D.C.

DEAR SENATOR PACKWOOD: The substantive language of the Louisiana Unfair Trade Practices and Consumer Protection Act mirrors the language of the Federal Trade Commission Act, as does the language of many other state consumer protection statutes.

I am concerned that certain proposed changes in the FTC Act definitions of unfairness and deception may make enforcement of state consumer protection laws more difficult.

I understand that the current proposals result from a desire to insure that federal resources are employed to best advantage. My own staff employs criteria similar to those proposed in evaluating our consumer protection cases.

However, I believe it would be a mistake to take case selection criteria and make them elements of unlawful conduct so that they become part of the government's burden of proof, as the current proposals would do.

This is particularly true where, as here, the suggested changes introduce uncertain concepts, such as substantial or material injury and cost benefit analysis, which might be read into state law courts which treat Federal Trade Commission case law as persuasive.

Enclosed for your reference is a resolution, approved unanimously by the Executive Committee of the National Association of Attorneys General, urging that changes in the FTC Act which would impact state law by subject to extensive study, and opposing altogether changes that would undermine the ability of state officials to protect consumers.[1]

I urge you to oppose amendments to Section 5(a) of the FTC Act at this time.

Very truly yours,

WILLIAM J. GUSTE, Jr.,
Attorney General.

NATIONAL ASSOCIATION OF ATTORNEYS GENERAL,
Washington, D.C. May 4, 1982.

MEMORANDUM

To: Members, Senate Commerce, Science and Transportation Committee.

We are informed that the Commerce Committee may soon consider the FTC reauthorization, including possible amendments to Section 5(a) of the Federal Trade Commission Act, which would change the FTC's jurisdiction over unfair or deceptive acts or practices. This matter is of great interest to the state Attorneys General, since virtually every state, in statutes modeled on the federal law, prohibits deceptive practices while numerous other states also prohibit unfair acts or practices. Because most state courts rely on Commission and federal court interpretations of the FTC Act, changes to Section 5(a) could have widespread effects on consumer protection enforcement in the states.

I am writing to your attention the enclosed resolution that the Association's Executive Committee adopted on March 28, opposing any amendments to Section 5(a) of the FTC Act that would undercut consumer protection enforcement in the states. If Congress wishes to consider these kinds of proposals that will impact on state laws, we urge you to subject these proposed changes, prior to enactment, to extensive study and review in consultation with Attorneys General and other affected state officials. The current version of Section 5(a) has been a feature of the FTC Act for 44 years, and any modification of this section deserves careful scrutiny before any changes are made. We would be glad to cooperate with you in a study of these issues. Please feel free to call me or my deputy, Lynne Ross, if we can be of further assistance.

Sincerely,

C. RAYMOND MARVIN.

Enclosure.

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[1] The enclosure referred to is printed as part of the comments of the National Association of Attorneys General.

NATIONAL ASSOCIATION OF ATTORNEYS GENERAL EXECUTIVE COMMITTEE MEETING

FTC AUTHORIZATION

Whereas, the Congress in considering amendments to Section 5(a) of the Federal Trade Commission Act, which would change the FTC's jurisdiction over deceptive or unfair acts or practices; and

Whereas, such amendments include the codification of cost-benefit analysis, which is an appropriate policy making tool in the development of unfairness cases but is unnecessarily restrictive as the standard to be used in all cases; and various restrictive and unwarranted changes in the definition of deception; and

Whereas, an amendment providing an exemption for commercial speech beyond the First Amendment exemption is unnecessary in light of the existence of a well developed body of case law that has already resolved this issue; and

Whereas, consumer protection statutes of 33 states mirror the FTC's bar against "unfair or deceptive acts or practices," and 13 others declare deceptive practices to be unlawful; (see attached table); and

Whereas, 20 state statutes explicitly say state courts should follow Commission and federal court interpretations of the FTC Act and where statutes don't contain this explicit directive, most state courts have interpreted state statutes consistently with the FTC Act; and

Whereas, if the FTC Act is changed, it may moot case law already developed in the states and further, will throw the state consumer protection statutes into a period of great uncertainty; and

Whereas, these changes have been proposed without consultation with state officials;

Now therefore be it resolved that the National Association of Attorneys General:

1. Opposes any amendments to Section 5(a) of the FTC Act that would circumscribe the scope of consumer protection statutes at the state level and would undermine the ability of states to protect their citizens; and

2. Urges the Congress that if it wishes to amend the FTC Act in such a way that will impact on state law, these changes should be subject to extensive study and consultation with state governors, legislators, and Attorneys General prior to enactment.

3. Authorizes its General Counsel to transmit these views to the appropriate members of the Administration and Congress.

Approved unanimously by the Executive Committee.

LOCKER GREENBERG & BRAININ, P.C.,
New York, N.Y., May 7, 1982.

CONSUMER SUBCOMMITTEE OF THE SENATE COMMITTEE ON COMMERCE,
Dirksen Senate Office Building,
Washington, D.C.

GENTLEMEN: We represent the Toy Manufacturers of America, Inc. ("TMA"), a non-profit trade association whose membership accounts for approximately 90 percent of the toy industry's 4.2 billion dollars in annual sales volume at the wholesale level.

The subcommittee is currently considering legislation as a part of its bi-annual oversight and authorizing review of the Federal Trade Commission. The FTC Improvements Act of 1980 will expire in September of this year. TMA believes that the 1980 Act should be extended, particularly its moratorium on rulemaking proceedings based upon "unfair" commercial advertising. TMA also believes that the Commission's jurisdiction over "unfair" acts or practices should be restricted to commercial practices, and should be delineated by appropriate standards.

Section 5 of the Federal Trade Commission Act provides broad, undefined authority for FTC action:

"Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are declared unlawful."

Section 5(b)(6) of the Act empowers the FTC to identify and prohibit such practices on a piecemeal basis. Section 18(a)(1)(B) empowers the Commission to promulgate rules that specify acts or practices which are unfair or deceptive under Section 5. Pursuant to the FTC Improvements Act of 1980, there is a two-year moratorium on such rulemaking proceedings based upon "unfair" commercial advertising.

Traditionally, the FTC has directed is regulatory efforts in two main directions: prohibiting the practices which interfere with competition, and preventing the use of deceptive practices. In the past decade, however, the Commission has turned its attention to business activities which are neither anti-competitive nor deceptive, as those terms have been traditionally used. Even more recently, the FTC has regulated practices which involved neither unfair commercial practices nor false or deceptive advertising. Through Section 5 proceedings, the FTC has banned advertising that, while not deceptive, was thought to be "unfair" by the Commission. The use of the Commission's power to declare advertising and other commercial practices that it deemed "unfair" to be illegal reached its zenith in the childrens' advertising proceeding where the Commission sought to use its broad, Section 18(a)(1)(B) rulemaking power to ban all television advertising which, although not deceptive, the Commission though to be per se "unfair". That proceeding led to Congressional action to restructure the proceeding (FTC Improvements Act of 1980, Section 11(a)(1)).

During this growth in the use of the "unfair" terminology of the Federal Trade Commission Act, the courts have shown little interest in curbing the broad discretionary powers of the FTC. In *FTC* v. *Sperry & Hutchinson Co.* (405 U.S. 233 [1972]), the Supreme Court gave the Commission the apparent unlimited authority to "like a court of equity, consider public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws" in deciding what unfair practices were (405 U.S. at 244).

The broad discretion of the Commission to declare an act to be "unfair" has not been effectively delineated by any standards. Although in *Sperry & Hutchinson*, the court delineated three factors to be weighed in making such a finding, the Commission's staff has stated that a practice could be found to be unfair "without specifically measuring it against any of the three [factors]" (Introduction and Recommendations and Summary; The Promulgation of a Trade Rule Regulating Television Advertising at 31–32). Thus, although some factors have been alluded to, they have been diluted and sometimes discarded by the FTC.

"Unfairness" is an extremely vague criterion for determining those practices which the FTC has the authority to prohibit. Unlike deception, a finding of unfairness goes beyond questions of fact, and involves normative values. A determination that particular practices are unfair to consumers necessarily involves matters of general public policy. When the "unfairness" criterion is used in the area of advertising, the Commission is allowed to make public policy decisions over what commercial speech can contain, and to whom it may be broadcast. These "public policy" decisions will, of necessity, involve decisions outside of the Commission's area of expertise. (In the childrens' advertising proceeding, the Commission attempted to weigh the psychological ability of children to understand advertising).

This use by the FTC of the power to declare, without objective guidance, certain advertising to be unfair threatens to impair First Amendment rights. In *Virginia State Board of Pharmacy* v. *Citizens of Consumer Council, Inc.*, (425 U.S. 748 [1976]), the Supreme Court held that a State statute that prohibited certain advertising by pharmacists violated the First Amendment, since its effect was to suppress "concededly truthful information about entirely lawful activity . . ." (Id. at 773). As the Supreme Court recognized, while the regulation of false or deceptive commercial speech is permissible under the First Amendment, regulation that impedes the free flow of truthful and non-deceptive speech is not. By assuming the authority to decide that particular commercial speech, although truthful and non-deceptive, is somehow "unfair" and should be banned, the Commission is intruding into an area protected by the First Amendment (see Senate Report No. 96–500 at 17).

In addition, when that power to declare advertising "unfair" is used in the context of a Section 5 proceeding, it violates due process requirements of fair notice as to what acts are prescribed by law. When the power to declare certain non-deceptive advertising "unfair" is used under the rulemaking powers of the Magnuson/Moss Act, it allows the Commission to establish wide-ranging norms for society beyond its expertise.

In light of this, the Federal Trade Commission Act should clearly delineate what types of acts and commercial practices may be prescribed under the heading of "unfairness" and what factors should be weighed in making such decisions. Because the FTC is an independent commission, principal responsibility for its oversight and control lies with Congress. The courts have often noted the failure of Congress to further define "unfair" in approving broad discretion for the Commission (*FTC* v. *Sperry & Hutchinson Co.*, supra).

TMA recommends that Congress act to end the Commission's authority to prohibit "unfair" advertising practices under both Section 5 and Section 18 of the FTC Act. TMA recognizes our society's need to have the Commission regulate "unfair" commercial practices as opposed to advertising practices. Such activities do not infringe upon constitutionally protected speech. They also usually involve areas of the Commission's expertise. As to "unfair" commercial practices, Congress should delineate the factors the Commission must weigh in making such a determination. TMA recognizes the legitimate interest of the FTC in continuing its present regulation of false or deceptive advertisements as the term "false" or "deceptive" is traditionally defined. However, the Commission cannot be allowed to regulate advertising which is in its opinion "unfair."

Congress could carry out these recommendations through the following actions:

1. Continue the current moratorium on Section 18 rulemaking proceedings directed at "unfair" commercial advertising as provided in Section 11 of the FTC's Improvements Act of 1980.

2. The passage of legislation withdrawing the Commission's power to declare any commercial advertising which is not "false of deceptive" unfair pursuant to Section 5 of the FTC Act.

3. The passage of appropriate legislation delineating what factors must be weighed by the Commission before it makes any finding under either Section 5 or Section 18 that any commercial practice is "unfair." The factors should include: (i) foreseeable substantial consumer injury; (ii) inability of consumers to reasonably avoid such injury; (iii) the conduct in question should have net detrimental effects upon either consumers or competition generally (the conduct in question is not outweighed by countervailing benefits or costs).

Such legislation would curb the Commission's discretion while allowing it to deal with truly unfair or deceptive practices.

Very truly yours,

AARON LOCKER.

THE STATE OF NEW HAMPSHIRE,
THE ATTORNEY GENERAL,
Concord, N.H., May 7, 1982.

Hon. ROBERT PACKWOOD,
U.S. Senator,
Russell Building, Washington, D.C.

DEAR SENATOR PACKWOOD: I would like to take this opportunity to reaffirm my opposition to any amendments of Section 5(a) of the Federal Trade Commission Act that might circumscribe the scope of state consumer protection statutes and limit the ability of states to protect their citizens from unfair and deceptive acts or practices. The reasons for this opposition have already been outlined in a Resolution approved unanimously by The Executive Committee of the National Association of Attorneys General at their March 28-30, 1982, meeting and forwarded to members of Congress. A copy of this Resolution is enclosed for your information.[1] I also endorese the Executive Committee recommendation to the Congress that all proposed amendments be submitted to state governors, legislators and Attorneys General for extensive study prior to enactment.

The State of New Hampshire is one of many states that has adopted the "mini-FTC Act" as its primary Consumer Protection Act (N.H. RSA 358-A). Our law, which has been liberally construed by state courts, prohibits both "unfair" and "deceptive" acts or practices and contains an express provision setting forth the intent of the legislature that state courts be guided by the interpretation and construction given Section 5(a) of the federal FTC Act (See RSA 358-A:13). Accordingly, I have significant concern that any limitations placed on the scope of the federal act, which are not based on a thorough analysis of related state laws, may have an adverse impact on consumer rights and remedies at the state level.

Thank you for your attention to these concerns. If you are in need of additional information, we would be pleased to provide it for you.

Very truly yours,

GREGORY H. SMITH,
Attorney General.

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[1] The enclosure referred to is printed as part of the Comments of the National Association of Attorneys General.

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